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OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

COMPLETED

HEARINGS

BEFORE THE

SUBCOMMITTEE ON
POSTSECONDARY EDUCATION

OF THE

COMMITTEE ON EDUCATION AND LABOR
HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

SECOND SESSION

HEARINGS HELD IN WASHINGTON, D.C., ON JANUARY 27, 28;
FEBRUARY 2, 3, AND 4, 1982

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OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

WEDNESDAY, JANUARY 27, 1982

House of Representatives,
Subcommittee on Postsecondary Education,
Committee on Education and Labor,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room 2257, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Ford, Peyser, Weiss, Erdahl, and Bailey.

Staff present: William A. Blakey, majority counsel, and John Dean, minority counsel.

Mr. Simon. The subcommittee hearing will come to order. The Subcommittee on Postsecondary Education begins 5 days of oversight hearings today on the major Federal student assistance programs.

This is the first time since the enactment of the Education Amendments of 1980 that we have taken a comprehensive look at the administration and operation of these programs which are so critical to the realization of the postsecondary education dreams of so many Americans.

Several other factors make these oversight hearings appropriate at this time:

First, current cost constraints necessitate congressional review to insure both administrative efficiency in the Education Department and on the campus, and to guarantee that the target populations are being served. We are talking about those who otherwise would not be able to have educational opportunity.

Second, several internal department studies, General Accounting Office reports and the semiannual report of the Inspector General have outlined concerns and problems which require subcommittee review and action, if appropriate.

Third, many in the higher education community have explored thoughtful solutions to the issues raised in these reports and we want to give them an opportunity to share their views with the subcommittee.

Finally, many of the changes in our student aid programs—enacted in the haste of our consideration of the Omnibus Budget Reconciliation Act of 1981—also need reexamination.

The new dollar limitations placed on the Pell grant, supplemental educational opportunity grants, college work study and the national direct student loan program are of special concern to me.

The potential impact of these reductions on the poor, the educationally disadvantaged, students from families whose parents work hard every day to make a living wage, and public and private institutions across America could be devastating in the short run and disastrous in the long run.

I think it is the feeling of most of us on this subcommittee, if not all of us, that we have to make sure all of those who desire to expand their educational horizons through higher education have that opportunity.

I will enter my full statement in the record.

[The prepared statement of Paul Simon follows:]

PREPARED STATEMENT OF HON. PAUL SIMON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS, CHAIRMAN, SUBCOMMITTEE ON POSTSECONDARY EDUCATION

The Subcommittee on Postsecondary Education begins five days of oversight hearings today on the major Federal student assistant programs. This is the first time since the enactment of the Education Amendments of 1980 that we have taken a comprehensive look at the administration and operation of these programs which are so critical to the realization of the postsecondary education dreams of many low and middle income Americans.

Several other factors make these oversight hearings appropriate at this time:

First, current cost constraints necessitate congressional review to ensure both administrative efficiency in the Education Department and on the campus, and to guarantee that the target populations have been served.

Second, several internal Department studies, General Accounting Office reports and the semi-annual report of the Inspector General have outlined concerns and problems which require Subcommittee review and action, where appropriate.

Third, many in the higher education community have explored thoughtful solutions to the issues raised in these reports and we want to give them an opportunity to share their views with the Subcommittee.

Finally, many of the changes in our student aid programs—enacted in the haste of our consideration of the Omnibus Budget Reconciliation Act of 1981—also need re-examination. The new dollar limitations placed on the Pell Grant, Supplemental Educational Opportunity Grants, College Work Study and the National Direct Student Loan program are of special concern to me. The potential impact of these reductions on the poor, the educationally-disadvantaged, students from families whose parents work hard everyday to make a living wage, and public and private institutions across America could be devastating in the short run and disastrous in the long run. Federal student aid, which has grown in the recent past, is declining at the same time the cost of attaining a college education rises:

In fiscal year 1979, 6,117,991 awards were made with expenditures of $3,211,350,908;

In fiscal year 1980 6,824,954 awards were made with expenditures of $5,890,528,765;

In fiscal year 1981 7,707,152 awards were made with expenditures of $7,255,825,762;

For the current year it is estimated that 8,900,000 awards will be made but expenditures will decrease to $6,065,750,000.

Because I believe the opportunity to attend college should be available to all regardless of income, race or sex, where you live or who your parents happen to be, I will continue to support the continuation of a significant Federal role in postsecondary education. I, for one, don't believe that whether you live in Michigan, Mississippi or Montana should determine whether or not you go to college. The role of Federal assistance in postsecondary education has had positive effects. The Federal government first became involved because states and local governments did not and could not provide necessary services. Shirking our responsibility and sending it to the states is not providing leadership. Nor will it solve the problem.

Our witnesses today are the Inspector General of the Department of Education, James B. Thomas, and the Deputy Assistant Secretary for Student Financial Assistance Dr. Elmendorf and his associates.

Mr. **Simon**. Mr. Peyser, do you care to add anything?

Mr. **Peyser**. No, not at this time.

Mr. **Simon**. Mr. Bailey?

Mr. **Bailey**. No comment, thank you.

Mr. **Simon**. Mr. Erdahl?

Mr. **Erdahl**. I am here to listen and learn, too. Thank you, Mr. Chairman.

Mr. **Simon**. I don't know what the witnesses have done to our subcommittee.

Mr. Ford, do you wish to add anything?

Mr. **Ford**. No, sir, I am here to hear what is going to happen to it.

Mr. **Simon**. That is an unusually silent subcommittee. That will not prevail very long, but we shall proceed with our witnesses.

First the Inspector General, James B. Thomas, Jr.

STATEMENT OF JAMES B. THOMAS, JR., INSPECTOR GENERAL, DEPARTMENT OF EDUCATION, ACCOMPANIED BY JOHN C. YAZURLO.

Mr. **Simon**. We are pleased to have you with us here today, Mr. Thomas.

Mr. **Thomas**. Thank you, Mr. Chairman, members of the committee. I have with me John C. Yazurlo, Assistant Inspector General for Audits in the Department of Education.

I am pleased to be here today to provide you with an overview——

Mr. **Erdahl**. I think some people in the back of the room have difficulty hearing.

Mr. **Simon**. It doesn't sound like the mikes are on.

Mr. **Thomas**. I am here to provide you with an overview of the Office of Inspector General activity as it relates to the postsecondary education programs, especially in the student financial aid area.

The OIG shares the committee's concerns as to how well the Department is administering its student assistance programs and how effectively they are being implemented by postsecondary educational institutions.

This is especially true in view of the magnitude of expenditures for postsecondary education. We recognized early that we would have to devote a significant portion of our audit and investigative resources to reviews of postsecondary programs, especially those related to student financial aid.

To date, our audit and investigative efforts in this important area have been fruitful and have contributed both to improved economy and efficiency in the administration of the programs and to the reduction of fraud, waste and mismanagement.

In fiscal year 1981, we issued 4,811 audit reports on postsecondary education programs. Costs disallowed or questioned amounted to $25.3 million. The vast majority of these reviews were financial and compliance audits of the campus-based and Pell grant programs performed by independent public accountants.

These audits were made in accordance with audit guides developed by the Office of Inspector General. Quality assurance reviews are selectively performed by OIG auditors of the actual work performed by independent public accountants to insure that the work meets auditing standards established by the Comptroller General and OIG audit guides.

In fiscal year 1981, the OIG used a significant portion of its audit staff resources on postsecondary education programs. Our fiscal year 1982 audit plan provides for approximately 42 staff years or about 25 percent of all available audit resources to review postsecondary programs.

This time will be spent on both external and internal audits, including reviewing audit reports prepared by independent public accountants.

Additionally, a significant amount of our investigative resources were devoted to conducting investigations dealing with abuses in student financial aid programs.

Departmental management has generally been responsive to recommendations stemming from our audits and investigations and has initiated appropriate actions to strengthen the programs and/or to recover improperly expended funds.

Some of our more significant audit results achieved during 1981 follow.

An audit of a State guarantee agency disclosed that the Department paid about $346,000 in excess interest because of differing interest computation methods allowed by current regulations.

Projections of the audit results nationwide indicated that the Department may have paid as much as $4 million in excess interest over a 4-year period.

A review of cash management practices by postsecondary schools in one region disclosed that about $11.6 million in excess Federal cash was being maintained by schools administering student financial assistance programs.

The auditors estimated that this excessive cash retention cost the Federal Government $1.3 million in interest in this region alone in fiscal year 1980. Projecting these results nationwide suggests that about $11 million in excess interest costs may be involved.

BACKLOG OF AUDITS

The backlog of unresolved student financial aid audit reports has been a continuing concern of the Department. However, during the last 4 months, exceptional progress has been made.

As of December 31, 1981, the Office of Postsecondary Education had 1,365 unresolved audit reports on hand.

I might add only about 500 were over 6 months old.

Questioned costs on the reports which remained unresolved totaled $23.8 million. Questioned costs sustained by program managers and marked for recovery amounted to $10.4 million during fiscal year 1981.

The OIG is in the process of establishing a formal audit resolution system which will involve the Department's top managers and which should further improve the timeliness and effectiveness of the resolution process.

Since the inception of OIG, our investigators have presented about 118 cases to the Department of Justice for potential prosecution which involved student financial assistance programs.

Of these cases, 72 were accepted by the prosecutors for prosecution. To date, 58 indictments have been returned and 45 individuals have either negotiated guilty pleas or have been convicted.

Typically, these cases involved the submission of false data or misapplication and/or embezzlement of funds. The following examples of investigations depict some of the schemes which have been used to defraud student financial assistance programs.

In a plea agreement accepted by the Federal District Court of Colorado, the Bell & Howell Co. pled guilty to three counts of false statements and one count of mail fraud.

Bell & Howell will be subject to a fine of $31,000 by the agreement.

The company pled that it lied to the Government in its handling of default claims submitted under the guaranteed student loan program. Significantly, the plea agreement also stipulates a civil settlement with the Department of Education by which Bell & Howell will pay $3.75 million.

The Department of Justice will continue with the prosecution of two former Bell & Howell employees indicted as a result of an investigation by our office and the U.S. Postal Inspector Service.

A former college financial aid officer was indicted by a Federal grand jury in August 1981, on 16 counts of embezzlement and false statements.

The financial aid officer falsified approximately $4,700 in Pell grant checks to students and then converted the checks for personal use.

The president of a proprietary school pled guilty to one count of aiding and abetting as part of a scheme to defraud the Pell grant program. The criminal counts related to 134 Pell grants and approximately $19,000 were diverted to the defendant's personal use.

The defendant was sentenced to 6 months' incarceration, 2½ years' probation, and restitution of the misapplied funds.

I appreciate you asking me here today and I will be happy to answer questions.

Mr. SIMON. Thank you very much.

When you say costs disallowed or questioned to $25.3 million, can you separate those two?

Mr. THOMAS. Not in the accounting system that we have, Mr. Chairman. Generally speaking, the same report may have both what we would call disallowed costs and questioned costs, so it comes out in a lump sum.

Mr. SIMON. It seems to me, maybe the system needs to be altered or else the terms need to be altered, because the cost disallowed or questioned seems to me to be quite possibly of variance.

On the—you are familiar with the GAO report on NDSL?

Mr. THOMAS. We have seen that report, yes, sir. We are generally familiar with it.

Mr. SIMON. On that NDSL report, they talked about a high default rate of 16.04 percent as of June 30, 1979. Has that improved since that time? Do you know, or is this not something that you—is it within the purview of your responsibilities as Inspector General?

Mr. THOMAS. Well, it is an area of interest, Congressman, but not an area that I am in a position to answer for you now.

I think perhaps Mr. Elmendorf might be able to do that.

Mr. SIMON. Well, we will get to our next witness on that.

Mr. Ford?

Mr. FORD. Thank you, Mr. Chairman. I would like to get back to your question, if I have time. But, first, looking at the paragraph entitled "Activities in 1981," I think it is page 2 of your statement, which states, "additionally a significant amount of our investigative resources were devoted to conducting investigations dealing with abuses in student financial aid programs."

Generally, when we have heard the use of the term "abuses," it is associated with an abuse by an institution or a student beneficiary or their family in the sense that money is misapplied, the common phony story about the kids buying sports cars with student loans and so on.

Then, having said that, and having devoted all of this effort to your study you come up later with three specific examples of what you were talking about, all of which actually amount to violations of—clear violations of the law, one by a major American corporation, one by a college official, and one by the president of a private proprietary school corporation.

Does that—is it safe to assume from that that you didn't really find any abuses of the programs, but you found some people stealing money from the Government?

Mr. THOMAS. I would have to answer that, Congressman, in that we found both. We have both abuses and we have occasions of people stealing money.

Mr. FORD. Again, it is the same thing raised by the chairman. We have a little problem in semantics, perhaps, but if you look at the record of years of consideration on these programs and oversight over them, by the Congress, and previous administrations, then just look at the kind of material that gets into the print in other media, you get the impression there are widespread abuses that need to be addressed, that have to do with the deliberate acts of evasion by students or beneficiaries of the program.

None of the people you are talking about here who have pled guilty are beneficiaries of the program by virtue of being the people for whom the program is intended.

Bell & Howell certainly is not a student. The college financial aid officer, a simple case of plain, clean, embezzlement.

It happened to be the only thing that that thief could steal was Pell grant money, but he is nevertheless characterized by your description here as a thief, who stole something that happened to be student aid. It didn't have anything to do with abusing the program.

The next one is the president of a proprietary school who apparently falsified some kind of information to qualify somebody to receive some kind of money, you are not at all specific about it, except to say that it related to 134 Pell grants.

What I am interested in is it is believed by some people in this city and certainly by spokespersons for the administration that there is rampant in the Government abuse of Federal programs, fraud and abuse is generally referred to.

One of the programs they tick off all of the time in a general sense is student aid. I note that apropos of the chairman's question, when you talk about cost disallowed or questioned amounting to 25.3 million, you then qualify by saying the vast majority of these reviews were financial and compliance audits of the campus-based and Pell grant programs.

Inasmuch as you spend all of this time looking for fraud and abuse, and using your own words, devoted a major portion of your resources to it, don't you have some examples of students ripping off the system you can tell us about?

Mr. THOMAS. Yes, sir. The items listed in the prepared testimony, Congressman, just to try to illustrate some of these different cases.

We have in the latest semiannual report sent to Congress a laundry list of the types of cases that we had and I would be happy to go through some of those, if it would help.

Mr. FORD. Let's see if we can get to students abusing the program. Tell me how often you found abuse and what kind you found?

Mr. THOMAS. We have a case in the Northeast of an individual getting guaranteed student loans by using a fictitious name and social security and birthdates. A series of loans by falsifying the application forms.

Mr. FORD. Hasn't he, by what you said, committed at least two and possibly three felonies?

Mr. THOMAS. Yes, sir. And has been sentenced for that and gone to jail. It is a student.

Mr. FORD. That is not some kind of fraud and abuse going undiscovered and unhandled, we have this jasper in jail, don't we?

Mr. THOMAS. We have that particular one, yes, sir. If I can characterize perhaps a group that happened in the State of Rhode Island, we had a joint investigation there with the Immigration and Naturalization Service.

We were concerned about illegal aliens taking advantage of both the grant and the loan program and, working with the U.S. attorney, we had a single case which resulted in indicting 27 individuals, in one locale.

We presently have a major project going on concerning illegal aliens taking advantage of these programs, who are not eligible in other parts of the country and we should be seeing the fruits of that investigation in the not-too-distant future.

Mr. FORD. You are saying that some aliens have been sneaking into Rhode Island to get a college education? Were they legally in the country?

Mr. THOMAS. I beg your pardon?

Mr. FORD. Were they legally in the country?

Mr. THOMAS. Illegally in the country.

Mr. FORD. Whether they are legally or illegally in the country, they might not be eligible anyhow because we do have very strange citizenship requirements in some of the programs. What kind of program were they ripping off?

Mr. THOMAS. This particular one was Pell grant and guaranteed student loans; 27 individuals we are talking about here.

Mr. **Ford**. They got the guaranteed loans by telling the bankers that—or not revealing to the banker that they had sneaked across the border?

Mr. **Thomas**. Yes, sir.

Mr. **Ford**. Maybe I shouldn't make that assumption. These weren't Haitians and Cubans, were they?

Mr. **Thomas**. No, sir, they were not.

Mr. **Ford**. Where did they come from?

Mr. **Thomas**. Most of this particular group of 27 individuals came from two or three countries in Africa.

Mr. **Ford**. Where else in the country do you expect to find the additional people in this classification? You said that you have a continuing investigation going with Immigration people?

Mr. **Thomas**. Yes, sir.

Mr. **Ford**. How are you going about that?

Mr. **Thomas**. We are working with the universities and we are working with the Immigration people to try to ascertain whether the individuals are, in fact, qualified for the student grant program by being a citizen or by being—I think the term is, having an adequate green card.

Mr. **Ford**. What if they are a permanent resident?

Mr. **Thomas**. I can't tell you all of the details of eligibility off the top of my head. But the case here is that these people are clearly ineligible for the program.

Mr. **Ford**. Without trying to be impolite to you, the American public is entitled to get to the bottom of this. We created a Commission last year to look at student aid programs. I have been more than a little distressed in the recent years with the number of instant experts who write in broad-bushed strokes about all of the fraud and abuse that goes on in these programs.

You are telling me out of all of these resources you use, you have been trying to find out who is a legal resident and you have been concentrating time on trying to find that kind of abuse?

Mr. **Thomas**. That is one of the areas we are looking at, where we have had——

Mr. **Ford**. How much have you produced for the Government out of this investigation?

Mr. **Thomas**. We have 27 people who have been indicted, I believe about 19 of whom have been convicted at this point in time.

Mr. **Ford**. Did you recover any money for the Government?

Mr. **Thomas**. Not from those, no, sir. Hopefully we will have avoided paying those individuals loans and grants in the following years by having caught them early in their efforts.

Mr. **Ford**. Tell me about another kind of student abuse.

Mr. **Thomas**. We have one situation which is an ongoing investigation now, which we have some early results in where individuals are falsifying applications for Pell grants and it works something like this: An individual will go on the college campus and look for students and tell those students that he will help you get a grant. They will take the information from the student, fill out the application form.

The application form will go in, the student will receive back an eligibility review form. They will then go and get the grant.

The grant will then be shared with the person who helped the student falsify the application report.

We are presently working in three or four States on this particular activity.

Mr. **Ford**. What is the violation involved in that case you just mentioned?

Mr. **Thomas**. Falsifying a document and getting benefits to which people are not entitled.

Mr. **Ford**. You have not prosecuted that case?

Mr. **Thomas**. We have not prosecuted the case.

Mr. **Ford**. The people doing the falsifying here and the person that is getting the illegal benefits is not the student, it is some third-party hustler?

Mr. **Thomas**. They are both illegally getting the funds.

Mr. **Ford**. The student, to the extent that the student was conned into believing he needed help to get the grant, participated in this, but the illegal benefit that inured to somebody who shouldn't receive it was the other guy, wasn't it?

Mr. **Thomas**. They bought it illegally, Congressman. Whether or not the person was conned into it or whether or not he was aware is subjective, I think.

Mr. **Ford**. If they picked a poor fellow off of the campus who had all of the characteristics of an eligible Pell grant recipient and had him fill out the application and presented it for him and then took a cut for the service performed, how did he get the Pell grant if he didn't have the proper characteristics to be entitled to it?

Mr. **Thomas**. He falsified the statement. The person that filled out the——

Mr. **Ford**. He did not, indeed, have the characteristics—

Mr. **Thomas**. Did not have the characteristics of an eligible recipient, yes.

Mr. **Ford**. Was he a student?

Mr. **Thomas**. Yes, sir. Was not otherwise eligible without falsifying the application.

Mr. **Ford**. How many cases like this have you run across?

Mr. **Thomas**. This investigation is ongoing in three States.

Mr. **Ford**. How many people like this have you found?

Mr. **Thomas**. We have found one person perpetrating this fraud. He has a series of people located on different college campuses that are helping him; then you have that branched out into the students who are either willing or unwilling participants.

Mr. **Ford**. You have not litigated this case, so we are just talking, and obviously we don't know where it is or who the people are, so it is going to be some kind of a proceeding.

Can you give me any other kinds of instances of students abusing the program? It is students who abuse it that I really want to go after, you understand. Because those are the people that we read about all of the time.

Mr. **Thomas**. We have, with a particular case, an individual that pled guilty to fraudulently obtaining a $2,500 guaranteed student loan.

We have now found that that person has been involved in a series of such fraudulent activity at different universities and we have also found that in this same type of thing, there are as many as 13 additional people being pursued at the present time—the continuation of the same investigation.

Mr. **Ford**. This person who fraudulently obtained more than one student loan or a student loan, what was the element of fraud involved? Did he lie about his family income? Did he lie about being a student in attendance at the college, or did he lie about how he was going to use the money?

Mr. **Thomas**. I don't have that information in front of me, Congressman. I apologize for that.

Mr. **Ford**. You see, that seems to me to be exactly what is at the core of what this committee has to do. If we do not have adequate safeguards in the law at the present time to prevent fraud and abuse, we ought to be legislating them.

It is not very helpful if you say in some general way this person got a bad guaranteed student loan but you don't know what is bad about it. You don't know whether they lied about their status as a student, with respect to the institution, their qualifications with respect to the family income, or, in fact, if they used a phony name or whatever?

Mr. **Thomas**. We have that information. I just don't have it in front of me.

Mr. **Ford**. How many of those kinds of things have you run into?

Mr. **Thomas**. I don't have a number, I have an example that happened during this last 6-month period.

Mr. **Ford**. Do you have more than one?

Mr. **Thomas**.v I don't have more than one, other than what I listed here.

Mr. **Ford**. I have gone well beyond my time, I apologize to members of the committee. I would like to come back later.

Mr. **Simon**. Mr. Erdahl.

Mr. **Erdahl**. Thank you, Mr Chairman, I was just going to ask the gentleman from Michigan to yield in his little jousting match here, because I think what we are getting at is the stereotype, that many people from the media report when they talk about fraud, abuse in the student loan program and the defaults.

My understanding, I think, that many people have is that an eligible student gets either a Pell Grant or a guaranteed student loan and then, to use the vernacular, the kid bugs out and doesn't repay the loan.

I think that is a common assumption many people have. I think the administration gives that impression. I think the media does. I take it you have picked some isolated cases to make examples and I accept them as such, but what can you tell us about the eligible recipients of the loans, who just don't bother to pay them back?

I would assume that is the real big part of the whole problem? Am I right?

Mr. **Thomas**. That is a part of the problem; yes, sir. I think that the people who are following me here would be in a better position than I to address that particular issue.

We are, 2 or 3 years ago, the Department of Health, Education and Welfare did a match program trying to identify those people who worked for the Federal Government, who had loans but had not repaid them.

They found a large number. We presently are in the process of getting ready to do that again, trying to identify people who are in a particular program, namely Federal employees who have these loans and are not repaying them so we can make extra efforts to make collections.

In addition to that, there is the normal collection effort which the student financial-aid program people are going about and which they now have contracts with outside contractors to pursue.

So they are intensified in the last year or so, they have intensified significantly the effort for trying to make those collections.

Mr. **Erdahl**. Could you tell us what the magnitude of those defaults might be? Or maybe we have other witnesses yet this afternoon that would supply that information?

Mr. **Thomas**. If I may, I would just like to defer to the witnesses following. I am sure they could provide that to you.

I don't have it in front of me.

Mr. **Erdahl**. I happen to endorse the concept that we should not abandon the guaranteed student loan program or the Pell Grants. I commonly give the example of the local banker back home; if he has trouble in collecting or with loans, he doesn't quit making them. He does a better job of collecting.

I think we have the mechanism in this country even though it is tough to use the Federal income tax and maybe there are legal questions involved in all of that, but it seems to me we are defrauding not only the Government, but also the bona fide recipients of the program if we don't do a better job on collecting the loans.

Later on today, maybe we will find out how to deal with that program.

Mr. **Thomas**. I think one of the significant things the Department has been doing recently has been to issue proposed regulations putting a little more pressure on the institutions to do a better job in this collection process.

I think those regulations are now outstanding and I am sure they will be discussed later.

Mr. **Ford**. Will the gentleman yield for a moment?

Mr. **Erdahl**. Yes.

Mr. **Ford**. It seems to me the last Congress, we specifically changed the law to authorize the Internal Revenue Department to give the Department of Education the last known address that Internal Revenue has on the student-loan person who is in default.

Is that being used?

Mr. **Thomas**. I think it is being used in the collection process.

Mr. **Ford**. Thank you.

Mr. **Erdahl**. Mr. Chairman, just one other question. One of the things that I had thought about, we also talked about that last session. I wasn't sure if it is being implemented or not. One of the examples in your report concerns a rather large company and involves a considerable amount of money. Good auditing in such situations would be one that is cost-effective for the Government.

The question I would have is how does your Department stand as far as available personnel. We hear of some reductions in Government employees. Are your auditors being RIFed, I guess to use a word around this town, reduction in force?

Is that going to be a problem?

Mr. THOMAS. My auditors are not presently being RIFed, Congressman. We started this calendar year with a staff of about 302. Our ceiling at that point was about 304 total staff.

At the present time, our onboard staff is 272, so we are down about 30 people, roughly 10 percent. The continuing resolution with the cuts, as we are now carrying it out, will require that my staff go down in the vicinity of 255 to 260 in order for me to continue to carry out any kind of an operation.

Because of the severe problem that we are having with onboard staff, relative to the amount of money available, I have now instructed my regional inspectors general that when they finish the current audits they have outstanding, that they are presently working on away from their duty station, they are to return to their duty station, and try to find audits to be done at the duty station because we cannot afford to continue to pay travel costs.

Mr. ERDAHL. I think that raises very serious questions because I think your brief report here makes an argument for the success of your operation. I think that most of us and certainly on this committee who are committed to maintaining adequate student programs would also be committed to rooting out, to use the term we hear around this town, any fraud, waste, mismanagement that occurs.

Can they do the job if they are restricted to home base, so to speak? I would think it would be essential that they be out in the field to do their job?

Mr. THOMAS. They have to go where the problems are, Congressman.

Mr. ERDAHL. I thought you just said you were going to tell them that they can't travel at all.

Mr. THOMAS. I have to, I can't pay them and it is a criminal penalty if I spend more funds than I have available. Consequently, they will have to do audits at the site where they are located, even though those are not the primary targets of where we found problems that exist.

Mr. ERDAHL. I think you have outlined a very serious problem, not one of your making. I hope that someone else in the committee or myself follows up on this last point because I think it is rather critical.

Mr. SIMON. Mr. Peyser.

Mr. PEYSER. Thank you, Mr. Chairman. I was just thinking as I was listening to you about the inability of getting your people out that this is a part of the President's program on volunteerism. We could run an ad and ask these people to come in who have been abusive.

Mr. ERDAHL. I think you are heading for the President's cabinet.

Mr. PEYSER. Well, you know, seriously, I am upset. I read the report and I have listened to your comments and I am trying to figure out what your office has really done that relates to the problem. I looked down at the bottom the next-to-last page which says, cases referred to the Department of Justice.

I assume this is of a culmination of the work that your organization has been doing. It says that 118 cases have been presented to the Department of Justice, of which 72 were accepted, so I gather that means 43 were not considered worthy of prosecution. Of the

72, 58 indictments have been returned and 45 have negotiated guilty pleas or been convicted.

Can you break down, of that group, whether these were students who had somehow cheated the Government in these programs or whether these were financial-aid officers, members of financial institutions or how does that of the group that we come down to, does this figure of 45 break down as to who was who? What is the percentage of students and what is the percentage of other people, financial aid people or college presidents, or whoever else has been cheating the Government?

Mr. THOMAS. I don't have a breakdown of those numbers exactly, Congressman. Of the 58 indictments, the majority have been students. I say the majority simply because, in the one case, we had the 27 illegal aliens.

Mr. PEYSER. Are they included in that group?

Mr. THOMAS. They are included in that group.

Mr. PEYSER. So if you took the 27 out of there, you are really down to 31 other people?

Mr. THOMAS. That's correct.

Mr. PEYSER. Out of the 31 other people, what would you say the percentage of students are?

Mr. THOMAS. The percentage of students is, it would just be a guess on my part, I will venture a guess to say perhaps 25 or 30 percent. One of the things that we find is that an individual student, an individual student, even though he or she commits a fraudulent loan in a one-time case, they are generally not prosecuted.

This is so of those cases that were not exempted from prosecution. The U.S. attorney, in looking at his or her priority schedule, generally will not prosecute a single student for a single fraud.

Mr. PEYSER. Well, let me ask a question.

In your opinion, having done this investigation and even though it is still ongoing, do you feel that based on what you have uncovered, that there are flagrant student violations of the Federal grant programs and guaranteed student loans based on what you know now?

In other words, let's start off with flagrant and if you don't think they are flagrant maybe we can define it down into another word that would be more understandable or more acceptable.

How would you categorize it based on what you know?

Mr. THOMAS. I would say that from the information that we have available and the investigations that we either have completed or in process that there are a large number.

Flagrant, I think, would probably be an overstatement.

Mr. PEYSER. How would you qualify large number? Would you want to put a percent figure on it?

Mr. THOMAS. No, sir. There would be no way for me to do that, Congressman, because the only cases of fraud or abuse that we have are those that we know about.

Mr. PEYSER. Is there a pattern? Because you know, I believe, that you have a little over 5 million students involved in the Federal grant programs and the guaranteed student loan program.

And, as Mr. Ford mentioned before, the image that has been created by the administration's statements is that out of these 5 million people ripping us off.

The rich kids are ripping us off, the poor kids are ripping us off, and the program is like a sieve. We are not getting anything back.

Now, we have never been able on this committee to find information to substantiate that belief and in reading your report, I certainly don't get the feeling on the cases that you are citing and on the information you are giving. Where you cite one student here, and one student there and there are aliens that are cheating us, and that this is something we can condemn a program over.

I mean I don't get that at all. Maybe I am misreading what you are saying here but I understand you have nearly 90 people assigned to working on this. Is that correct?

You indicate 25 percent of your staff is involved here and you mention 370-some people, so I assume that maybe you have 90 of your people involved in this investigation?

Mr. THOMAS. Of the city investigation; no, sir.

Mr. PEYSER. How many people were involved in putting the investigation together?

Mr. THOMAS. You are talking about the investigation of the illegal aliens?

Mr. PEYSER. Oh, no, about everything. Of all the 172 cases that we have come up with that the Justice Department has taken, I gather that there has been a lot of investigating going on.

I am trying to find out how much investigating.

Mr. THOMAS. We have a nationwide staff, including management and secretarial and investigators of about 70.

Mr. PEYSER. So 70 people have been involved full time in this operation?

Mr. THOMAS. That is correct.

Mr. PEYSER. And out of all of those people and all that work that is going on we seem to be coming up for each one of them we have got one case that has been accepted by the Justice Department.

My feeling is that there is not a great deal out there. You say a large number and say 70 people, over how long a period of time has this investigation been going on for all of these things?

Mr. THOMAS. We have been in business since May of 1980 and I came to the Department in the fall of 1980 and that is when we began to put the staff together.

Mr. PEYSER. So for nearly 18 or 20 months, with 70 people working full time with the whole country involved, with over 5 million students under the program, not counting other student aid programs, it seems to me like we have come up with a handful of cases, and these are people who are not just abusing. They are lawbreakers, people who are outright breaking the law and doing it with full knowledge of what they are doing.

I think if that is the case, Mr. Chairman, we are doing much better than I thought we might have been doing on these programs.

Mr. SIMON. Would my colleague yield?

Mr. PEYSER. I will be glad to.

Mr. SIMON. Let me follow up.

As I read the costs disallowed and questioned, I assume when you say questioned these are things where there is a question of what is right or wrong, it amounts for the fiscal year to $25.3 million.

Since the total program costs about $6.4 billion we are talking about less than one-third of 1 percent of the total when we talk about costs disallowed or questioned.

Now, that does not include the student default problem, I recognize.

From your experience in other departments or as you talked to other Inspectors General, it strikes me that this may be an exceptionally good record rather than one that we should hang our head in shame about. Or am I reaching some conclusions that I should not reach?

Mr. THOMAS. I don't think you are reaching conclusions that you should not, Congressman. I think that the dollar amounts that are showed are the result of audits for a 1-year period that have been done primarily by independent public accountants of the student aid programs.

The numbers that you have recited, the $25.3 million, reflect that effort.

Mr. SIMON. Thank you.

Mr. Bailey.

Mr. BAILEY. I have a couple of questions for you, Mr. Inspector General. And I would like to preface this by telling you that we have had some rather heated discussions on the committee concerning misapplied or that word in the law that seems to indicate that a substantially wealthy person might obtain funding for their college student and instead of applying that to the college student's education might simply buy money market funds in order to take advantage of the low cost.

And we have made certain changes in the law during the last session through the resolutions among much wailing and moaning about whether the remaining need or income limits should be applied.

As Inspector General do you look at income limits or remaining needs as an aid in inspection toward misapplication of funds or is that misapplication so difficult to determine that with your 70 people nationwide you have to really go after the larger cases?

Would you care to comment about that?

Mr. THOMAS. The investigations that we have done are primarily the result of some kind of allegation that we have received of wrongdoing. And as a consequence, generally speaking, there has been a reason to believe on somebody's part that there is something wrong before the case comes to our attention.

The 70 people that you mentioned and I believe Mr. Peyser mentioned earlier relate to the number of people that we have through all the programs not just the student aid program, although the majority of the staff is involved in the student aid activity.

Mr. BAILEY. Do you have other activities that you are working on in addition to these?

Mr. THOMAS. Yes; that is right.

Mr. BAILEY. And as you indicated, you cooperate with the Justice Department. You really don't have time, manpower or incentives to go after individual people where it might be very, very difficult to prove that they misapplied money, whether they really were applying this money as people indicated, whether they bought a sports car with or not, even though that is the intent?

You don't have the tools to accomplish that, do you?

Mr. **Thomas.** It seems to me, Congressman, that there may be two issues here that you are dealing with.

Let me see if I can separate them in my own mind. If we did not have an indication that a person obtained the funds through an illegal process then we probably would not look at how the funds were spent at all as part of our investigative effort.

So it would only be in followup of the person who had gotten those funds illegally that we would be involved in a specific student loan or grant. And our concern there would be primarily on whether or not there is any criminal act committed by that individuals obtaining those funds from the federal system as opposed to where those funds were used.

Now, as a general rule we would not have gone out to look at a case and see whether or not a person had used the money for money market certificates or for a sports car unless there was an indication that he had obtained those funds in an illegal fashion. That is not the kind of thing that we would normally do.

Mr. **Bailey.** And that, I think, is of substantial public concern about the college program.

Thank you for your comments. I hope that if you uncover during your investigation of these large numbers of doubtful claimants that your inspection procedures indicate better reforms that we can make.

I hope that you will continue to indicate those to this committee.

Thank you very much.

Thank you, Mr. Chairman.

Mr. **Simon.** Mr. Weiss?

Mr. **Weiss.** Thank you very much, Mr. Chairman.

Mr. Inspector General, is the investigation or followup on default at all touched upon by your department or is that handled by other people?

Mr. **Thomas.** That is generally handled by other people. We would do an internal evaluation as part of the process of internal audit. We have not yet done that.

Mr. **Weiss.** I think that the reason that you are feeling some expressions of frustration is not because of your work but because of the political use to which this whole issue has been put, allegations made without substance, distortions, so that when you read the headline you get one impression.

You read the story in the press and you get an entirely different impression.

As far as I am concerned within the realm that you have been assigned to do work, you are doing good work. And what you, I think, are demonstrating, and you can tell me if I am correct, is that which has invariably come forth in all the IG investigations which is that the bulk of the fraud is not by the recipients, that is the heavy fraud, the fraud that costs money, but by some element of providers or third parties who decide that they are going to get in the gravy. And that, in essence, is what you have found as far as the cases that you have sent to the Justice Department as far as the dollar value of the cases that you referred, is not that so?

Mr. **Thomas.** I would say that is very definitely so; yes, sir.

We have focused, in some cases, on the institution, on a particular proprietary school that has abused the system and, therefore, all the students or the majority of the students for that institution. And those are the kinds of cases that we have worked with with the Justice Department. Those are the cases which have taken the largest portion of our staff effort.

Mr. **Weiss.** The *Bell & Howell* case, it is hard to really understand what that case is about but apparently almost $4 million is being returned to the Government that was improperly gained by that company or officers of that company; is that correct?

Mr. **Thomas.** Yes, sir.

Mr. **Weiss.** And through some kind of fraudulent or inappropriate illegal means, yes?

Mr. **Thomas.** Yes.

Mr. **Weiss.** And then you cite some examples of problems and I am shocked that in the first instance the excess interest was taken by the State guarantee agency because it was, in your words, "allowed by current regulations."

So that was not an abuse of the system but a vagueness in the regulations which appropriately and properly allowed that agency to choose whichever system was more beneficial to it; is that correct?

Mr. **Thomas.** That is correct. They were options of different kinds of processes and the agency to whom the loans were sold used one and the one to whom the loan was made used another and it resulted in different results for a period of time.

Mr. **Weiss.** And it is perfectly within the law and you have made recommendations to tighten that up so it does not continue?

Mr. **Thomas.** That is right.

Mr. **Weiss.** And the last item, the cash management practices apparently you say there may be $11 million in excess interest costs involved.

I assume that that, too, was money that was retained properly but to the detriment of the Federal Government; is that correct?

Mr. **Thomas.** It was obtained properly in one context. Even though there are rules that say you should only draw down a short period of time for usage and, in fact, greater amounts were drawn down. So as far as an illegal act it was not an illegal act. It was a judgment call, I would say.

Mr. **Weiss.** Right.

Mr. **Thomas.** That report has not been issued yet. We have issued drafts and generally the management of the department supports the recommendations that they are making and we anticipate that this will be tightened up.

Mr. **Weiss.** Have you had discussions, incidentally, within the department as to what happens to your operation upon dismantling of the department?

Mr. **Thomas.** It is my understanding that a decision has not been made as to exactly what kind of reorganization will come about. In my formal discussions I have an indication that if there is a new educational organization that there will be an Office of the Inspector General within such an organization.

Mr. **Ford**. Will the gentleman yield?

Mr. **Weiss**. I would be pleased to yield.

Mr. **Ford**. After reading the other day that there are some $600 million this year in oil and gas royalties that were not paid on Indian lands and other Government-owned property that maybe the Interior Department could use your 70 investigators over there because you could really collect some money for us if we put you over there.

Thank you.

Mr. **Weiss**. Together with the Department of Education?

Mr. **Ford**. Well, they are not making much money here but it looks like you could pick it up by the hundreds of millions over at Interior if you catch these guys who are plugged into our Indian lands and not paying for the oil.

Mr. **Bailey**. We will call it the Oil and Gas and Indian Education Foundation.

Mr. **Weiss**. But I gather that they are scheduled for elimination, too. So maybe you will go into business for yourselves, I don't know.

Thank you, Mr. Chairman.

Mr. **Simon**. Mr. Thomas, if I may just follow up on the last question by Mr. Weiss, this $11 million in excess interest, in your report I note that you refer to this as caused by poor cash management practices in student financial aid programs.

From your observation of personnel we have in these programs operating like this, do we have a good balance, and I hope the bookkeepers in here will forgive me, between hard-nosed bookkeepers and education policymakers in the office so that we can avoid this kind of a mistake?

I would just be interested in your impression.

Mr. **Thomas**. I don't have any reason to think otherwise, Congressman. You are talking about now, in the department?

Mr. **Simon**. Yes.

Mr. **Thomas**. The people that I have been working with have expressed an extreme amount of interest in taking actions and they demonstrate to me the ability to take those actions so I don't have any reason to think otherwise than what you said.

Mr. **Simon**. Have you, in any way, received any political pressure to do or not to do things as an Inspector General? It is just a very general question.

Mr. **Thomas**. Absolutely not; no, sir.

Mr. **Simon**. Then, finally, and this has nothing to do with the immediate questions in front of us but one of the bills that is before this subcommittee is one that affects DQ University, an Indian university in California.

My understanding is that you have some studies going on regarding that institution. Are you at liberty at this point to indicate what those studies show or can you indicate how soon the subcommittee can have the results of those studies?

Mr. **Thomas**. The basic field work, Mr. Chairman, has now been completed and the staff is in the process of bringing together a draft report.

My feeling is that until such time as we have had them bring together that draft report to make sure that the points are well stated and well founded that at that time we will be giving a draft of that to the auditee, in this case DQ University, for them to go over and make sure that they do not have any additional information which we did not have access to or did not consider in our audit process.

And once we get that information then we would be happy and willing to sit down with you or your staff and share with you the results of that.

Mr. SIMON. So we are talking about 6 weeks, roughly, or what kind of timeframe?

Mr. THOMAS. I would say around 6 weeks would be satisfactory.

Mr. SIMON. Mr. Ford?

Mr. FORD. The first question is, have you encountered any abuse of the student financial aid programs that you have not been able to reach legally?

In other words, do we have any gaps in the law? Is it possible to abuse the program and not violate the law?

Mr. THOMAS. Off the top of my head, Congressman, I can't think of anything that would fit that category.

Mr. FORD. Well, one of the problems we have and I have read the sections of the law to so many Members of Congress that I really ought to remember it.

On October 3, 1980, we added to title 20 United States Code, section 1097 Criminal Penalties, and made it a felony, as a matter of fact, for people to do the kind of things that have been described in your examples even when those things would also be a violation of State laws such as the embezzlement you talked about.

Obviously, the person who did the embezzling could have been prosecuted in the State courts without the Federal statute but the statute says that:

> Any person knowingly and willfully embezzles, misapplies, steals or obtains by fraud, false statement or forgery, funds, assets or property provided or insured under this Title shall be fined not more than $10,000 or imprisoned for not more than five years, or both.

I still find that as a result of new people in the administration assuming that no one in Washington ever cared before they got here whether people violated the law or not that they don't know that it is a felony to do the things that they say are being done on a wholesale basis out there by young people who are abusing the program.

And if you run across a case where you see an abuse and the U.S. attorney is telling you that we have not got tough enough with 5 years in prison and $10,000, I hope you will let us know so we can toughen the law up, because Mr. Simon and I are two of the great law and order members of this body.

In your report submitted earlier, the semiannual report to Congress, after reviewing the numbers of things that you were doing in the Office of the Inspector General, on page 23 you have a heading:

> STUDENT FINANCIAL ASSISTANCE
>
> Student Financial Assistance programs are administered by the Office of Education to provide financial aid for individuals or training beyond a high school level.

Financial aid provided in 1981 represented about $6.4 billion in grants, interest on loans, guaranteed loans and earnings on work study programs.

Then you go on to enumerate the problems that you found, the first one, (a) different interest computation methods in excess of interest payment and you indicate that the Department of Education paid $346,000 in excess interest during the period April 1977 to September 1980 because of the different interest computation methods used by the lenders and the Student Loan Marketing Association of this State.

We estimate that as much as $4 million in excess payments may have been made nationwide from 1975 to 1979, $4 million over 4 years. But, nevertheless, that appears to be an auditor's quibble about how bankers compute interest, something that would probably be incomprehensible to me if you tried to explain it to me.

"(b) Poor cash management practices in student financial aid programs resulted in unnecessary interest costs of $1.3 million.

"(c) Abuse of student financial assistance programs by two proprietary colleges resulted in termination and proposed fines of $3 million."

And then, "(d), erroneous interests of $2 million paid by ED. The Education Department erroneously paid lending institutions $2 million in interest for loans that they paid to the Student Aid Marketing Association."

Again, it sounds like the bankers and auditors are quibbling about what is right. They don't allege any illegal activities here. It appears that the administrative errors here cost far more than any of the cases you have enumerated with respect to fraud and embezzlement.

That, indeed, the argument about the interest rate differences here totaled more millions of dollars than all of the cases you have enumerated of people who have been discovered to have deliberately stolen from the program.

"(e), ED. overpaid State agency $2 million for losses on defaults of guaranteed student loans."

Again, an argument between the State-guaranteeing agency and the Office of Education on what the proper amounts would be.

What I find here is in this report not one single mention of the misapplication of funds such as Mr. Bailey mentioned a few moments ago as one of the things I came across.

Although in this report you do talk about the 27 aliens and it is interesting that today you talk about them as illegal aliens but in your report to the Congress you did not call them illegal aliens, you called them nonresident aliens.

Can you tell me what the difference between an illegal alien or a nonresident alien is with respect to the student aid program?

Mr. THOMAS. No, sir; I guess I can't. I am not sure that there is a technical difference in the terminology that was used there.

Mr. FORD. Well, there certainly is a technical difference. It happens every day in my district. I have Canadians who drive legally across the bridge every day and work at the Ford Motor Co. Well, they did when we were still making cars.

But before the depression, people drove from Canada every day to work. They had a green card. They are nonresident aliens but they are legal aliens and you are using artful terms. You are the No. 1 Inspector General over there.

These are terms of art that even a lawyer as inexperienced as I am can recognize have some meaning, and it seems to me that if we have got a glitch in the law that lets people sneak across the border I had better be careful because I am right on the Canadian border and those people are going to be sneaking over getting an education at our expense.

Now, would you find out what the difference is between the time you filed this report in September when you referred to the 27 cases as nonresident aliens and now in your testimony to us and your formal statement you refer to them as illegal aliens and, indeed, does it make any difference if they are aliens whether they are nonresident or illegal with respect to getting the student loan?

I think that since you use that as one of your prime examples and the only one that has any substantial evidence of students themselves participating in a sort of massive effort—27 of them.

It has alarmed you enough so that you indicated earlier that you intend to pursue this problem to other parts of the country. I assume you are going to go to Buffalo, N.Y., and see how many people come across Niagara Falls and go to Buffalo Community College. And the University of Detroit and Wayne State University commuting by bus from Windsor all up and down our borders.

Most of the time we talk about illegal or nonresident aliens around this country you are talking about Mexicans, Cubans, Haitians and other kinds of people who tend to irritate some part of the population and certainly have got this administration upset. But in my part of the country the chances are 99 out of 100 that they are nice Canadians who up until now have been our friends and allies.

I wish that you would tell the committee, if not now then following the hearing, what the significance of illegal or nonresident aliens accessing this program really is.

Mr. THOMAS. All right, sir. I will provide that for you.

[The information follows:]

U.S. DEPARTMENT OF EDUCATION,
OFFICE OF INSPECTOR GENERAL,
February 26, 1982.

Hon. PAUL SIMON,
Chairman, Subcommittee on Postsecondary Education, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your letter of January 28, 1982, requesting additional information on the activities of my office relative to audits and investigations of student financial aid programs. The clarifying information you requested and specific answers to questions raised are attached.

Please excuse the delay in my response. Unfortunately, we did not receive your letter in this office until February 22, 1982.

Sincerely,

JAMES B. THOMAS, Jr.

Enclosure.

QUESTION FROM MR. SIMON

Question 1. What is the difference between "questioned" and "disallowed" expenditures? A definition of your use of each term would be helpful.

Answer. Questioned costs are costs incurred by a grantee or contractor on behalf of ED-funded activities but, because they lack adequate supporting documentation or written policies or procedures, etc., are questioned by the auditor. In other words, these are costs for which the auditor is unable to express an opinion regarding their eligibility or allowability. ED management officials must determine what action to take on the questioned costs based on the auditor's explanation of the finding as well as on subsequent evidence provided by the auditee that the costs were supportable and allowable under the program regulations. If costs questioned in an audit report are subsequently determined to be eligible by ED management, the costs will be reclassified as eligible and no financial adjustment will be required by the auditee. If, however, ED management officials determine that the questioned costs have not been properly supported or are in fact ineligible, the costs are recalssified as disallowed and steps taken by ED management to effect financial recovery of adjustment.

On the other hand, disallowed costs are costs incurred by grantees or contractors on behalf of ED-funded activities which are determined by the auditor to be clearly ineligible based on law, contractual agreements or ED, State or local agency policies and regulations. The auditor then recommends that ED management officials disallow the costs and effect financial recovery or adjustment.

QUESTION FROM MR. FORD

Question 1. What is the difference between "illegal" and "non-resident" as used in your testimony and the Semi-Annual Report to Congress? You should indicate how each definition relates to eligibility for or participation in title IV programs.

Answer. In the context of both the Semi-Annual Report and my testimony, the terms "non-resident and "illegal" were broadly used to describe non-immigrant aliens who were ineligible for Title IV program benefits.

Eligibility requirements for student financial aid are set forth in the 1981-1982 Federal Student Financial Aid Handbook. With respect to citizenship requirements essential provisions require that a student must be one of the following:

U.S. citizen; U.S. national; Have an I-151 or I-551 (Alien Registration; Receipt Card); Permanent resident of the Trust Territory of the Pacific Islands; Permanent resident of Northern Mariana Islands.

If a student is not in one of these categories, then the student must have one of the following documents from INS:

I-94 (Arrival-Departure Records) with one of the following endorsements: "adjustment applicant", "refugee", "conditional entrant", "indefinite parole"; Official documentation that he or she has been granted asylum in the U.S. or; Other proof from INS that he or she is in the U.S. for other than a temporary purpose.

In the cases referred to in both the Semi-Annual Report and my testimony, all aliens indicted were non-immigrant aliens (any alien whose reason for coming to the U.S. involves a temporary stay that will end when its purpose has been accomplished) at the time they filed their applications for Pell Grants and/or Guaranteed Student Loans and did not meet any of the elgibility requirements described above. They all falsely claimed to be U.S. citizens on their applications.

QUESTIONS FROM MR. ERDAHL

Question 1. During your testimony, you indicated that your staff has been reduced and your travel budget restricted. What additional reductions or travel restrictions do you anticipate as part of the fiscal year 1983 budget?

Answer. The staff reductions and travel restrictions referred to in my testimony relate to problems associated with the limited funding provided under the fiscal year 1982 continuing resolution. The President's March budget request included $12.9 million, 335 positions and adequate travel funds for our office. The revised budget included only $11.4 million and our OMB ceiling is 304. The continuing resolution, however, limits our funding to $11 million, 16 percent less than the March request. This condition required that we freeze hiring, curtail promotions, and significantly reduce necessary travel. Thus we have been unable to fill vacancies as they occurred or meet our travel needs. Our full time equivalent staff has decreased from 302 in January 1981 to 269 in February 1982. The fiscal year 1983 Departmental Budget provides 304 positions and an increase in travel funds.

Question 2. In your best judgment, how much staff and travel funds do you require to effectively carry out your responsibilities with respect to Education Department programs (assume no further changes in the programs)?

Answer. The fiscal year 1983 staffing level request of 304 is the same as our fiscal year 1981 and fiscal year 1982 levels. I believe this "hold steady" levels is appropriate in light of changes we know are coming. Aside from any possible changes in programs, coming changes include implementation of OMB Circular A-102, Attachment P, which establishes a single audit requirement for State and local government entities and provides that we build on these audits in any work we do. The impact on our staffing needs from A-102 will be unclear until we gain some experience with in. Changes coming also include those resulting from block grant legislation already passed for many Departmental programs. In terms of travel funds needed, we believe the $936,000 requested in our budget will be sufficient.

Question 3. Could you specify what part of that staff would focus on student aid programs?

Answer. Our fiscal year 1982 audit work plan provides for approximately 34 staff years of audit effort on student aid programs. This represents about 27 percent of our available audit resources. Based on the number of allegations received and cases opened last year, we plan to devote about 65 percent of our investigative resources to student aid programs. This represents approximately 42 staff years.

Other Questions

Question 1. You cited two separate cases where the Department made excessive payments to Guarantee agencies. Could you estimate for us how much money in excess payments is made to Guarantee agencies nationwide?

Answer. At the present time, we do not have a basis for estimating all excess payments made to Guarantee agencies nationwide. Where appropriate, however, we do project the results of individual audits to show nationwide impact. In one of the two cases cited, for example, we estimated that excess interest payments to Guarantee agencies nationwide may have totaled as much as $4 million over a four-year period.

Question 2. How many Guarantee agencies have you investigated? Do you have any current ongoing audits involving Guarantee agencies and the amounts of monies they receive from the Department of Education or collect?

Answer. We have issued audit reports on two Guarantee agencies. An audit report on a third Guarantee agency is in draft. We are currently doing audit field work at a fourth agency. Our work plan for fiscal year 1982 calls for audits of four more agencies; however, this number will probably be reduced because of the hiring freeze and travel restrictions. In the central office, we are reviewing the current need for advance funds provided to Guarantee agencies in the past.

Question 3. Overall do you have any estimate of how much money or what percent of total Federal monies going to institutions or Guarantee agencies are excessive? How much of this do you feel is deliberate fraud and abuse as compared to administrative inefficiencies and errors?

Answer. We do not have an overall estimate of excessive Federal monies that go to institutions or Guarantee agencies. However, regarding the Pell Grant program, a draft report prepared by an ED Contractor entitled "Quality in the Basic Grant Delivery System" identified widespread errors. This report indicated that 73 percent of all grant disbursements were in error and net disbursements to students included overawards of $572 million and underawards of $119 million or a total of $453 million in net overawards.

My personal belief is that the majority of all excess funds paid are probably the result of administrative inefficiencies and errors. However, the incidence of deliberate fraud and abuse may well be above tolerable levels. We do not at present have a scientific basis for providing estimates.

Question 4. Generally, how long does it take the Department to act upon your recommendations? How actively do you monitor whether or not your recommendations are being followed?

Answer. Generally, the Department is trying to close all audits within six months. As of January 31, 1981, 535 or 33 percent of the unresolved 1,617 reports on hand were over six months old. This represents a significant improvement over the 1,804 unresolved audits over six months old reported as of September 30, 1981 and reflects the Department's commitment to remedy this problem.

The Office of Inspector General has been actively monitoring the audit resolution process. In this regard, we provide the Secretary and the Under Secretary with monthly status reports on unresolved audits along with a brief analysis and aging schedule of all open audits. Additionally, where necessary, we specifically follow up with individual offices that are experiencing delays or difficulties in resolving old audits. Also, we are nearing completion of a formal audit resolution system which should further improve the timeliness with which audit reports are closed.

Question 5. Have you conducted any investigations into Pell Grant overawards? Do you plan to do such an audit in the near future?

Answer. We have not conducted any audits wholly devoted to the subject of Pell Grant overawards. We have, however, included audit steps to detect overawards in our audits of the student aid programs at institutions. Steps aimed at detecting overawards are also included in the audit guide for independent public accountants for use in their audits of institutions participating in the Pell Grant program. These audits are usually conducted biennially.

In addition, we are currently surveying Pell Grant application processing, award validation, payments to institutions, and related activities in the Office of Postsecondary Education. We will make a similar survey at the Systems Development Corporation, the contractor which processes applications and produces Student Eligibility Reports. In determining the specific scope of the subsequent audit of the corporation, we are considering the overaward problems cited in the draft report on "Quality in the Basic Grant Delivery System" mentioned above. We expect to begin the audit during the current fiscal year.

Mr. FORD. Thank you, Mr. Chairman.

Mr. SIMON. I might mention that we would like to submit some additional questions to you, Mr. Thomas, for entering in the record.

Mr. Erdahl?

Mr. ERDAHL. Mr. Chairman, I have no further questions at this time.

Mr. SIMON. Mr. Bailey?

Mr. BAILEY. No, thank you.

Mr. SIMON. Mr. Weiss?

Mr. WEISS. No, thank you, Mr. Chairman.

Mr. SIMON. We thank you very much, Mr. Thomas, for being here and for your testimony.

Mr. THOMAS. Thank you, sir.

Mr. SIMON. Dr. Edward Elmendorf, Deputy Assistant Secretary for Student Financial Assistance, accompanied by James W. Moore, Director of Student Financial Assistance Programs; William L. Moran, Chief of the Pell Grant Policy Section; Joseph Vignone, the Chief of the Basic Grants Branch; David Bayer, Chief of Guaranteed Student Loan Branch, and Richard Hastings, Director of the Division of Certification and Program Review.

Dr. Elmendorf, we are pleased to have you. You may read your statement or we can enter it in the record and you can summarize, however you wish to proceed.

[The prepared statement of Edward Elmendorf follows:]

PREPARED STATEMENT OF DR. EDWARD M. ELMENDORF, DEPUTY ASSISTANT SECRETARY, STUDENT FINANCIAL ASSISTANCE, ACCOMPANIED BY JAMES W. MOORE, DIRECTOR, STUDENT FINANCIAL ASSISTANCE PROGRAMS; RICHARD A. HASTINGS, ACTING DIRECTOR, DIVISION OF CERTIFICATION AND PROGRAM REVIEW; DAVID C. BAYER, CHIEF, GUARANTEED STUDENT LOAN BRANCH, DIVISION OF POLICY AND PROGRAM DEVELOPMENT; JOSEPH A. VIGNONE, CHIEF, BASIC GRANT BRANCH; AND WILLIAM L. MORAN, CHIEF, POLICY SECTION, BASIC GRANT BRANCH

I am pleased to have this opportunity to report to you on the status of our student assistance programs, and some of the management initiatives we have undertaken in the Office of Student Financial Assistance.

In this academic year we estimate that some 8,900,000 awards will have been made under OSFA administered programs with expenditures of $6,063,750,000. Let me bring you up to date on each of our major programs.

PELL GRANTS

The Pell Grant program has grown dramatically from a modest program begun in the 1973-74 academic year with an appropriation of $122.1 million which enabled grants to be made to 185,000 students. In the current year we expect to provide assistance to approximately 2.8 million students. The average award is expected to be $838, resulting in an estimated expenditure of $2.346 billion.

As the Subcommittee well knows, for a period early last year the processing system was stopped and applications were not processed, resulting in a huge backlog by the time processing was resumed. We can happily report that by mid-summer, the backlog had been depleted and processing has since proceeded at a normal pace.

We will begin processing applications for the coming school year within 4-6 weeks. A Family Contribution Schedule for the Pell Grant program was submitted October 16, 1981, and rejected by the Senate on December 10, 1981. The development of a new schedule was governed by provisions of the third continuing appropriation resolution for fiscal year 1982. That resolution, under which we are now operating, specifies that the 1982-83 Pell Grant Family Contribution Schedules shall be the same as the 1981-82 Schedules, with the exception of certain specified modifications. The Continuing Resolution also authorized the continued use of separate need analysis systems for the campus-based programs for the 1982-83 award year. The final regulations for the 1982-83 Pell Grant Family Contribution Schedules, reflecting the directives of the Continuing Resolution and the Resolution of Disapproval, were submitted to Congress on December 30, 1981, and published in the Federal Register on January 6, 1982.

Consistent with the authority granted in the Reconciliation legislation of last August, we will have a series of assessment rates on parental discretionary income. The rates will range in four steps from 11 percent for the first $5,000 to 25 percent for income above $15,000. The asset reserve has been raised for the parents of dependent students and for independent students who have dependents. As provided in the Senate's resolution, there will be a $25,000 asset reserve against other personal assets, and $80,000 against farm and/or business assets. However, the total asset reserve that a family can use will be limited to $100,000 against all of their assets. In addition, the family size offsets have been raised by 9.4 percent over those used in 1981-82 to reflect inflation.

Another major modification for 1982-83, consistent with the Senate resolution, is the exclusion of the student's Social Security benefits and veterans educational benefits paid under chapters 34 and 35 of title 38, United States Code, in determining a student's eligibility index. These benefits will, however, be considered in determining the amount of a student's Pell Grant, because the total of the student's Pell Grant, expected family contribution, Social Security, and VA benefits may not exceed the student's cost of attendance.

QUALITY CONTROL STUDY

The findings of a Departmental Quality Control Study indicate serious errors in Pell Grant awards. The study further indicates that most award errors are the result of inaccurate information reported on the application form. As the Committee knows, the student aid programs have traditionally relied on self-reported information—much of which is of an estimated or projected nature. Most of the errors, therefore, are not the result of willful and intentional fraud and abuse on the part of students and parents, but can be attributed to an application process with an inherently high probability of error.

The result, however, as found in our study, is that 44 percent of all recipients reported erroneous information which affected their award amounts by plus or minus two dollars or more. The total net overpayment attributable to erroneous application data for the 1980-81 academic year is $289 million. The reporting of items relating to family adjusted gross income was particulary error-prone.

As a first but significant step in correcting award errors, the Department proposes to expand current validation efforts to include the requirement that all eligible applicants submit copies of the 1040 tax forms relating to the Pell Grant application.

The effort will focus on two particularly error-prone items on the student application—adjusted gross income and taxes paid. The central processor will notify all applicants eligible on the basis of unverified data that they must submit appropriate 1040s to the institution they wish to attend. The institution will then check the application against the information on the 1040 and return the corrected information to the central processor for reprocessing in those cases where a significant discrepancy is found. Limiting the verification to only two items should serve to minimize the burden on institutions while at the same time achieve significant savings in the Pell Grant Program. We anticipate the proposal would yield approximately $129 million in savings from error reduction at a cost to the Federal Government of $5 million in central processing costs and $5.2 million in administrative allowances for education institutions.

We have requested that $5 million of the program funds made available under the Continuing Resolution be reprogrammed to pay for the additional central processing costs and that institutions receive an administrative allowance for $2.00 per verified application—approximately $5.2 million in aggregate—to compensate them for this verification effort. It should be noted that this request does not increase the overall funding level for the program—nor does it result in a significant reduction in individual student awards for academic year 1982-83. We would also note that we view this as an interim solution for the 1982-83 academic year. The Department's longer term proposals are currently being developed and we expect that they will be announced along with the fiscal year 1983 budget. We are hopeful that our request will be received favorably. The savings achieved from preventing these over-awards will allow additional and increased awards for students who truly need that assistance.

STATE STUDENT INCENTIVE GRANTS

We estimate that in this school year approximately 307,000 students will receive State grant awards averaging $500. It seems apparent that this program has truly fulfilled its incentive role. All states are now participating and this year total State grant payout will exceed $900 million of which only $76.75 million are Federal SSIG funds.

CAMPUS-BASED

During this academic year, more than $1.1 billion has been obligated under the three campus-based programs, the College Work-Study (CWS), the Supplemental Educational Opportunity Grant (SEOG), and the National Direct Student Loan (NDSL) programs. We estimate that these funds will assist approximately 1.5 million needy students at 4,300 colleges and universities.

Specifically, with funding of $550 million, we estimate some 990,000 students are being provided work opportunities under the CWS Program at 3,307 participating institutions. These students earned on an average, approximately $600 to assist in meeting their expenses of this school year. Four thousand, twenty-four schools are participating in the SEOG Program, with funding of $370 million. We estimate some 586,000 students have received grants averaging $600.

Also during academic year 1981-82 3,365 institutions received new Federal capital contributions under the NDSL program. We should note that 340 institutions requested no new Federal capital and have gone into voluntary revolving status. An additional 370 schools were denied new capital because of their failure to provide due diligence in loan collections. In all, a total of $761,881,000 was available from which we estimate over 790,000 students will have received loans this year.

We do continue to experience problems in collections. As the Committee knows, the GAO came out with a report last fall critical of the high default rate in the loan program. Earlier this month, proposed regulations were issued which would prevent schools with a default rate over 25 percent from getting new Federal capital, except under specific appeal criteria. This measure was taken to lessen the likelihood of loss of NDSL funds, to encourage institutions to better manage their loan funds, and to base awards on actual collection results rather than on institutional claims. We estimate that approximately 800 institutions have default rates exceeding 25 percent.

Under the terms of the proposed regulations, institutions may appeal the penalty if they can show that the figures do not reflect their current collection effort.

In the near future, we expect to issue two additional sets of regulations. The first would address due diligence requirements; the second would deal with loan assignment specifics; giving institutions clear cut procedures for submitting loan paper.

We would note that the complexity of program administration has increased with the changes in interest rates, cancellation provisions and other elements of the statute. While billing can be consolidated for the student, we cannot consolidate the loans because of the different terms. Consequently, institutions must maintain action on separate accounts on each loan made. We are consequently unable to eliminate the burden on institutions as we have to some extent for student borrowers.

GUARANTEED STUDENT LOANS

The Guaranteed Student Loan Program, the only entitlement program in our student aid portfolio, continues to grow—both in loan volume and cost to the government. For example, in fiscal year 1981, 3.5 million students obtained loans in the amount of $7.7 billion—a "whopping" 52 percent increase in the number of borrowers and a 60 percent increase in the amount borrowed. In program costs to the government, we have a similar situation. Fiscal year 1981 required $2.535 billion in appropriated funds, an increase of 58 percent over the prior year. And, unless further legislative changes are made very early this year, we project that $3,061 billion will be required this year, assuming that 91-day Treasury bills will average 11.73 percent for the rest of this year. We would note that with a portfolio of approximately $20 billion every one percent annual change in Treasury bill rates translates into $200 million in program costs. Obviously, in these days of economic stringency, we must examine ways to restrict these expenditures. We hope that working together we can come up with a legislative package to control the costs of this program.

A number of activities and problems in the GSL program warrant your attention. We have recently completed a preliminary study of the financial position of the 52 guarantee agencies that administer the GSL program in every State except Mississippi and North Dakota—and I am pleased to state that these two States expect to have guarantee agencies operational this spring. The incentives enacted into law in 1976 have worked. There were only 26 States with guarantee agency programs prior to the Education Amendments of 1976. But I think we have provided more than adequate funding to the agencies to pay their operating costs, build their reserves and cover their current default costs. In addition to Federal funding for these purposes, the agencies are permitted by Federal law to charge insurance premiums and they receive investment income on their reserve holdings. It is clear that many agencies can now pay their own way. We find it extremely difficult to recommend to the Congress, funding cuts that affect students and colleges while we continue to improve the agencies' reserves with more funds than they need. We have to look seriously at the way we are now supporting the guarantee agencies, especially in the area of their administrative expenses. A letter has just been sent to all agencies asking that they work with us in proposing solutions to this problem.

The Postsecondary Student Assistance Amendments of 1981 made two major changes to the PLUS Program. It allowed graduate or professional and independent undergraduate students to borrow under that program and also raised the interest rate to 14 percent for all new loans.

These new statutory changes to the PLUS program have resulted in some additional delays in some States in implementing the PLUS program. Program literature, applications, promissory notes, operating forms, computer software, among other things, had to be redesigned. In addition, the guarantee agencies had significant other new legislative changes to implement, most on rather short notice, and many of which required a major labor intensive effort. In order to maximize savings of Federal dollars, we had to ask that a very short time frame be provided before the new changes became effective. However, in doing so, we recognized that many administrative problems are created for program participants. In an ideal world, we would probably suggest considerably longer periods of time between enactment and implementation. Because so many students were able to obtain loans prior to the effective dates of the various new statutory provisions, the pressure for PLUS loans this academic year has, to a large extent, been minimized. However, as the full impact of these new changes are felt for the 1982-83 academic year, and especially if Congress quickly approves our new legislative proposals, the demand for the PLUS program in every State will rapidly escalate.

As of December 31, 1981, the PLUS program was in operation in 23 States. We anticipate that it will be operational in every State in time for the 1982-83 academic year. There are still a couple of States which require State legislative approval before they can implement the PLUS program. And frankly, there are a few States where the guarantee agency has been dragging its feet. Commercial lender participation and interest in the PLUS program is also a concern. Yet, for those who are familiar with the history of the GSL program, there was a lot of "foot dragging" by the States and commercial lenders in 1965 when the Higher Education Act was originally enacted. The loan volume and data on guarantee agency participation I quoted earlier vividly demonstrates that there is virtually no "foot dragging" today in the GSLP. A lot of people had to work very hard and Congress has also responded with numerous legislative changes to assure student access to GSLP loans. While it may require a similar effort to "sell" the PLUS program, we are convinced that this is the way to go and are dedicated to making that effort.

In another area—we plan to submit the GSLP Family Contribution Schedule to the Congress in the very near future. At the same time, this will be published in the Federal Register as a notice of proposed rulemaking for public comment. We expect to propose that, for 1982-83, we follow essentially the same procedures that are in effect for the current academic year: the school may use the same "needs test" that it uses for the campus-based student aid programs or it may use a short-form, table lookup which was developed very quickly last summer with a magnificent joint effort of Congressional staff, financial aid administrators, organizational and State representatives and our own staff. Because of the need to publish the Family Contribution Schedule as a final rule as soon as possible, we do not think it appropriate to make any significant changes to the current process. To do otherwise would not provide sufficient lead time to the schools. The only change will be to update the Table used in determining a family's financial contribution. However, for the 1983-84 year, we do expect to modify the current system. In order to provide adequate planning time we expect to publish both the 1982-83 and the 1983-84 Family Contribution Schedules at the same time. The same publication will include our proposed regulations relating to the verification of the borrower's adjusted gross family income. This is part of our effort to reduce fraud and abuse in the student aid programs.

And that brings up an additional point. The legislation governing the GSL program has been amended so often and has become so complex that virtually no one can comprehend it. One of the major goals of this Administration is deregulation. One of the major goals of the previous Administration was to write regulations in simple English. Neither of those laudable goals is possible in the GSLP with the complex legislative base we have to start from. There is much that could be done to simplify the law and I suspect we would be surprised how much "fraud and abuse" could be eliminated if we did. We would be pleased to work with you in an effort to clarify and simplify the law.

I would also like to highlight some of the measures we have taken and are taking to improve our administration of these programs and reduce the incidents of waste, fraud, and abuse.

SATISFACTORY PROGRESS

As you know the Higher Education Act requires that a student be maintaining satisfactory progress according to the standards and practices of the institution in the course of study he or she is pursuing in order to receive financial aid under the title IV student assistance programs. In a recently published GAO study, the lack of reasonable standards and adequate enforcement at many institutions is cited as a serious abuse of Federal student aid programs. In addition to cases in which institutions failed to enforce their published standards, this study cites the use of standards by institutions which do not adequately measure students' "progress" toward their educational objective. As an example, students at one of the institutions in the GAO study remain eligible for title IV aid according to the satisfactory policies of the institution although they are never required to attain the institution's 2.00 grade point average graduation requirement. As another example, at a studied institution due to the institution's policies allowing for excessive withdrawals, a student earned a total of only 14 credit hours during six full-time semesters for which she received $11,645 in title IV aid.

With the deletion in the Education Amendments of 1980 of the limitation on years of eligibility for aid from the Pell Grant and SEOG programs, the establishment and enforcement of reasonable satisfactory progress standards are increasingly critical. Therefore, regulations in this area are being developed to help ensure the integrity of the student aid programs without encroaching on the statutory prerogative of institutions to establish specific satisfactory progress standards.

Proposed standards were developed and approved by the American Council on Education, the National Association of Collegiate Registrars and Admissions Officers, and the National Association of Student Financial Aid Administrators to assist in the achievement of effective self-regulation by the higher education community.

The regulations we are developing would in general simply equate reasonable standards with the adherence to policies of good practice as developed and accepted by the education community. Adherence in general would be demonstrated by conformance with the standards of satisfactory progress set by the institution's nationally recognized accrediting agency which incorporate certain basic elements developed by the community. If no agency standards exist, or if an institution is not governed by an agency, the proposed regulation would require the institution to incorporate into its standards of satisfactory progress the basic elements developed by the postsecondary education community. This community-based initiative does not affect the institution's statutory prerogative to establish satisfactory progress standards but does provide guidelines to help ensure the integrity of the student aid programs.

PUBLIC-PRIVATE LOAN COLLECTION EFFORT

In March of last year, Secretary Bell announced plans to consolidate the Department's defaulted Federal Insured Student Loan (FISL) and National Direct Student

Loan (NDSL) collection efforts to just three of the ten Office of Student Financial Assistance regional offices, and initiate contract arrangements with private collection agencies to supplement this effort. This move was made after studies commissioned both by the previous Administration and this Administration found that private collectors were at least as successful as Federal collectors. The internal consolidation, which included all documentation transfers was completed in late fall of last year.

In late summer of 1981, the Department published a Request for Proposals. A number of agencies responded with proposals to meet these contract requirements. Proposals were reviewed over a two month period following the closing date; and in late December, contracts were awarded to Gulf Coast Services of Houston, Texas, for collection activities associated with the Atlanta and Chicago regional offices, and to Payco American of Columbus, Ohio for collection activity associated with the San Francisco regional office: These contracts will result in average commissions of 29¢ per dollar collected. The initial transfer of 60,000 FISL loans took place yesterday, January 26. During the first year of these contracts, the private agencies will receive at least 90,000 FISL loans and 48,000 NDSL loans. The average value on each of the FISL loans is $1,732.00 while the average dollar value of the NDSL loans is $850.

Regional collection activity in fiscal year 1981 for the FISL program produced $36,763,000 in recoveries, compared to $40,150,000 in fiscal year 1980 under full ten region activity. The NDSL program showed collections of $6,554,000 in fiscal year 1981 as compared to a total of $2,620,000 in fiscal year 1980. Under the consolidated regional structure, totals for fiscal year 1982 thus far show recovery figures of $1,300,000 in NDSL for the first quarter, and $9,554,000 for FISL.

The Department's consolidation collection effort using both private sector collection agencies and Federal collection forces began yesterday. The strategy to be employed will include initial regional office attempts at converting defaulted loans to current repayment status within 120 days of initiation. If conversion to repayment is not effected within this time period, accounts will immediately be eligible for transfer to the contracting agencies. These agencies will then have a 15 month period during which specified collection activities must be performed. At the conclusion of that time, those accounts not converted into repayment or otherwise resolved, will be retuned to the Department for final close-out activity. We will be monitoring this new collection effort very closely. Under the terms of the contracts, each contractor will have two of our Department personnel acting as on-site monitors. Their responsibilities will include resolution of any program-related problems in addition to ensuring that mandatory collection activities are performed by the contracting agency.

I would also note that we have an internal Collections Task Force at work looking at ways in which we might further improve our collections effort.

Finally, I would like to emphasize the fact that the Department of Education's responsibility for collecting defaulted student loans extends only to NDSLs which are assigned or referred by institutions and to GSLs which are made under direct Federal insurance—a program which is fast phasing out or which maybe assigned by guarantee agencies under a recent statutory provision. The bulk of the responsibility for collecting on defaulted NDSL accounts rests with the schools themselves, while GSL default collection responsibility rests with the State and private nonprofit guarantee agencies. We are keeping a close eye on the guarantee agency collection effort and we will be proposing regulations in the near future specifying the circumstances under which GSL default accounts will be assigned to the Department. We will also be proposing legislative changes allowing schools to assign NDSL accounts to the Department earlier than the two year period now required (allowing the Secretary to set such rules), and allowing Federal recoveries on NDSL defaults to be reused in the program itself. Currently, such NDSL collections must be turned over the Treasury Department, while Federal collectors and contractors are paid from GSL collections (thus unnecessarily increasing GSL costs).

AUDITS AND REVIEWS

As part of the general effort to prevent fraud and abuse, institutions participating in the Campus-Based programs were required, beginning in 1976–77, to have regular non-Federal audits of the programs completed at least once every two years. A similar requirement took effect for the Pell Grant Program in 1978–79. While this workload has placed a tremendous strain on our review staff, we can report that the number of audits closed rose from 643 in fiscal year 1978 to 1,800 in fiscal year 1981. Recoveries over the past four years have averaged $5 million per year. We are now working with the Inspector General to revise the Departmental audit processing procedures in order to focus attention on significant audit findings and reduce emphasis on minor types of findings. This will mean that OSFA can direct attention to audits with the more serious problems while the number of audit reports requiring action is kept within manageable levels.

In addition, our Program Review Branch has, since the spring of 1977, conducted 3,780 institutional program reviews, which have yielded an estimated $51,767,281 in liability due the Federal Government. In the spring of 1979 we also began conducting reviews of lending institutions. Two thousand, eight hundred, fourteen such reviews have yielded an estimated savings to the Federal Government of $24,454,649.

We would also note that since 1977, OSFA has executed 95 Limitation Agreements with program participants, initiated 64 termination actions and imposed Emergency Actions on 27 institutions to prevent the likelihood of substantial loss of funds to the Department. Since the authority to fine institutions became effective on October 3, 1980, we have also initiated fine actions against 12 institutions. OSFA has also been extremely successful for the past year in litigation and negotiation to protect the integrity of the Federal Insured Student Loan Program. Almost $5 million was recovered through these procedures. While the list of actions is in no way comprehensive, I may convey to you some sense of the scope of OSFA's management activities.

I trust that this testimony is responsive to the points raised in your letter of invitation. I would be pleased to respond to any futher questions you may have.

GSLP/AS January 1982

GSL STATISTICAL SUMMARY REPORT

GSLP LOAN VOLUME

	FY 81	FY 80	% change
#	3.5 million	2.3 million	+52
$	7.7 billion	4.8 billion	+60
Ave.	2.196	2,091	+5

NEW VOLUME FY 82 TREND

	FY 82 (1st QTR)*	FY 81 (1st QTR)	% change
#	616 thousand	673 thousand	-8
$	1.4 billion	1.4 billion	0
Ave.	2,266	2,051	+10

* Estimate based on volume data from FISLP and ten large guarantee agencies accounting for over 70% of anticipated volume.

PLUS LOAN VOLUME

	FY 81	FY 82 (to date)		Cumulative since inception
	Parents only	Parents	Students	
#	11,000	4,600	300	16,000
$	27,000,000	11,900,000	775,000	40,000,000
Ave.	2,454	2,587	2,583	2,500

STATUS OF PLUS PROGRAM OPERATIONS

23 o Guarantee Agencies in Operation (16 Agencies actually guaranteed PLUS Loans to parents. Of those 16 agencies, 9 agencies had student PLUS loans)
19 o Guarantee Agencies that will set up PLUS operations by 4/30/82
10 o Guarantee Agencies expected to set up PLUS operations after 4/30/82)
2 o Guarantee Agencies deciding not to have their own PLUS operations
54

G.A. SOURCES OF FUNDS & USES OF FUNDS REPORTED ON GUARANTEE AGENCY QUARTERLY REPORTS

	FY 81*	FY 80
Total Sources	$ 412 million	$ 277 million
Total Uses	$ 295 million	$ 219 million
Fiscal Year Excess over uses	$ 117 million	$ 58 million

GUARANTEE AGENCY HOLDINGS

	FY 81	FY 80
Cumulative Adjusted Funds Available at end of FY	$ 449 million*	$ 325 million

* California & Indiana not included in FY 81.

SALLIE MAE CONSOLIDATED LOAN VOLUME (OPTIONS PROGRAM)

	#	$	ave. $
1st QTR FY 82	158	1.8 million	11,671

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TABLE 8
BASIC EDUCATIONAL OPPORTUNITY GRANT PROGRAM
SUMMARY STATISTICS FOR THREE-YEAR REFERENCE

AWARD PERIOD

	1973-1974	1974-1975	1975-1976	1976-1977	1977-1978	1978-1979	1979-1980	1980-1981	1981-1982[4]
NUMBER OF APPLICANTS SUBMITTING OFFICIAL APPLICATIONS	512,000	1,304,077	2,220,237	2,940,379	3,044,047	3,000,303	4,108,716	4,872,884	4,656,000
NUMBER OF APPLICANTS SUBMITTING VALID APPLICATIONS	482,271	1,144,004	2,170,090	2,400,730	2,821,041	3,401,430	3,809,429	4,512,304	not available
NUMBER AND PERCENT OF QUALIFIED APPLICANTS	300,444 62.24%	683,000 59.24%	1,490,501 68.00%	2,050,043 62.00%	2,300,330 62.10%	2,720,083 67.30%	3,079,745 72.36	3,367,290 69.10%	not available
NUMBER AND PERCENT OF NON-QUALIFIED APPLICANTS	213,807 41.70%	432,436 33.14%	722,000 30.93%	1,180,470 32.00%	1,221,321 30.09%	1,152,029 30.10%	838,004 20.03	1,145,016 23.50%	not available
NUMBER AND PERCENT OF APPLICATIONS RETURNED FOR INSUFFICIENT DATA AND NEVER RE-SUBMITTED FOR PROCESSING	30,037 5.96%	100,703 14.07%	100,041 9.07%	301,001 8.00%	222,000 6.70%	402,020 12.40%	318,307 7.60	360,380 7.40%	not available
NUMBER OF APPLICANTS SUBMITTING UNOFFICIAL APPLICATIONS						300,330	290,910	385,974	not available
CLASSES OF ELIGIBLE APPLICANTS	FULL-TIME FRESHMEN	FULL-TIME FRESHMEN & SOPHOMORES	FRESHMEN SOPHOMORES JUNIORS	ALL UNDER-GRADUATES	ALL UNDER-GRADUATES	ALL UNDER-GRADUATES	ALL UNDER-GRADUATES	All Under-graduates	All Under-graduates
NUMBER OF ELIGIBLE APPLICANTS SELECTED FOR VALIDATION						610,303	332,118	325,040	not available
NUMBER OF RECIPIENTS	176,000	567,000	1,217,000	1,944,000	2,011,000	1,893,000	2,537,878	2,805,000[3]	2,800,000
TOTAL EXPENDITURES	$47,589,000	$360,303,000	$929,000,000	$1,470,444,000	$1,524,340,000	$1,600,047,000	2,384,911,291	$2,500,000,000[3]	$2,346,000,000
AVERAGE BASIC GRANT	$270	$630	$761	$759	$758	$825	907	$891	$838
MINIMUM BASIC GRANT	$50	$50	$200	$200	$200	$50	$200	$150	$120
MAXIMUM BASIC GRANT	$452	$1,400	$1,400	$1,400	$1,400	$1,600	$1,800	$1,750	$1,670

1. The percentages of Qualified Applicants and Non-Qualified Applicants and the percentage of Applications returned for Insufficient Data and Never Re-submitted to Processing add up to 100 percent.

2. The minimum Basic Grant for the 1974-75 and 1978-79 Award Periods was $50 due to reduced funding.

3. Estimate based on current available data.

4. Estimated end of year data for 1981-82.

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STATEMENT OF EDWARD M. ELMENDORF, DEPUTY ASSISTANT SECRETARY, STUDENT FINANCIAL ASSISTANCE, ACCOMPANIED BY JAMES W. MOORE, DIRECTOR, STUDENT FINANCIAL ASSISTANCE PROGRAMS; RICHARD A. HASTINGS, ACTING DIRECTOR, DIVISION OF CERTIFICATION AND PROGRAM REVIEW; DAVID C. BAYER, CHIEF, GUARANTEED STUDENT LOAN BRANCH, DIVISION OF POLICY AND PROGRAM DEVELOPMENT; JOSEPH A. VIGNONE, CHIEF, BASIC GRANT BRANCH; AND WILLIAM L. MORAN, CHIEF, POLICY SECTION, BASIC GRANT BRANCH

Mr. ELMENDORF. Thank you, Mr. Chairman, and thank you for the opportunity to appear before you and talk about some of the accomplishments in the student financial aid program.

I have only been in Washington for 5 months now and I came from an institution as a chief executive. I can see from where some of the questions you might ask are coming. I think I can also respond knowing we had in the Office of Student Financial Assistance some of the most complex programs I think are in Government today.

I think it is a tribute to some of the people around the table here that I have a much different impression of the kind of people who support our student aid programs.

They are dedicated, loyal professionals who care about students. They certainly operate under very difficult circumstances. I would say that they have problems which [illegible] outnumber the accomplishments in our written testimony [illegible] they certianly do not outweigh them.

I believe you have before you a written statement which I would ask you to include in the record.

Mr. SIMON. It will be entered in the record.

Mr. ELMENDORF. Thank you, sir.

We estimate that some 9 million awards will be made to students under the Office of Student Financial Aid administered programs with expenditures coming to approximately $6 billion.

In beginning I would sort of like to give you a feeling about what my philosophy is relative to student financial aid.

I think it is shared by more people than not. Basically I believe it is the parent and student responsibility to finance postsecondary education. They have that primary responsibility.

When the cost to attend an institution of postsecondary education, however, is greater than the parents' and students' ability to pay, I believe there is a role for the State and Federal Government.

In filling that role, what we are trying to do is seek the best way to combine the resources that we have to allow access to some form of postsecondary education. Secretary Bell has set in place a set of goals for us. I won't give you those goals in detail but I can simply say that they are simplification of programs, self-regulation where possible, consolidation when possible, cost-effectiveness and I could go on.

One of the first things we did was try to set forth for the Office of Student Financial Aid a simple understandable mission. Briefly paraphrased it is to administer our programs and to deliver in an accurate and timely way to rightful constituents the funds that you have entrusted to us.

The second part of that mission is to propose alternatives to this delivery of student financial aid programs to you.

We set forth a number of basic general goals. The first of these goals and the most important is the accurate and timely delivery of the programs you see discussed on pages 1 through 12 in the testimony. Those programs are: The Pell program, your campus-based program, the Guaranteed Student Loan program, the Parent Loan program, and the State Student Incentive Grant program.

On pages 12 through 19 our second goal is addressed and that is to focus on the reduction of waste, fraud, and abuse in our programs.

I am proud that in pages 12 through 19 we have some accomplishments that we are prepared to talk about today. Those accomplishments focus upon our ability to collect funds from students who have defaulted, to resolve audits prepared by institutions for use of student financial aid funds and to, in one way or another, the trust that you give us to manage the funds.

Given that introductory statement I would like now to introduce those people who are with me at the table.

Mr. Vignone, on my far left, is the policy branch chief for the Pell program. Mr. Moran is the section chief in the policy area for that program. Mr. Hastings is the division director for the Division of Certification and Program Review where most of our audits, program reviews, and validation efforts are focused.

Mr. Hastings is also on special assignment to me to coordinate the collections effort and to coordinate the validation effort that we would like to talk about a little bit later in the testimony.

On my right is Mr. Jim Moore who I am sure is no stranger to you. He is the Director of all Student Aid programs, my right hand, my left hand and sometimes my history because I don't have much of a history.

On his right, Mr. Dave Bayer, who I am sure you all know is the policy chief in the Student Loan program.

Mr. SIMON. Thank you very much.

You say on page 3 of your statement most of the errors are not the result of willful and intentional fraud and abuse on the part of students and parents but became attributed to an application process with an inherently high probability of error.

Students estimate what their family income will be?

Mr. ELMENDORF. Yes, sir.

Mr. SIMON. Have you done any sampling of what would happen if we used last year's income and last year's income tax statements?

Mr. ELMENDORF. I can have Mr. Vignone answer the specific question. Let me see if I can't give you an umbrella answer. When we talk about errors on the form of not being intentional fraud what we are talking about is two things. One is that the data submitted by students is self-reported That kind of information is inherently error prone.

The second thing and the point you are making is that we are asking a student to project into the future what it is that will happen. In one case we ask them to identify the number of brothers and sisters who will be in postsecondary education 6 months from the time they submit the application. That is an example of the kind of projection of information we are asking.

Mr. Vignone, could you answer the question?

Mr. VIGNONE. Mr. Simon, I think there may be some definition of terms needed. We do, in fact, ask for last year's income. That is, for 1982 we will be asking for the 1981 tax information.

I think the thrust of your question is addressed to those applicants who file after January 1 and before the family completes its income tax forms on the IRS deadline of April 15.

We have had some studies in the past that have shown that the closer we get to April 15, the better the quality of the data. And that is true on both sides of April 15. This is an indication that at about that time students and families have their IRS documents ready, easy access to them, and consequently use them to complete their application form.

As we move beyond that date, forms tend to get lost.

Mr. SIMON. What if you simply ask for a xeroxed copy or some evidence of what that previous income is and if you file between January and April that you go back to 1980 or a year before?

Mr. VIGNONE. Those two questions I believe Dr. Elmendorf will be addressing in the specifics of our proposal. One of the mainstays of our proposal for corrective action is to request a student to bring a copy of the IRS 1040 and 1040-A along with the student eligibility report when he goes to the school for payment.

Mr. SIMON. And I guess my only hesitancy there is what if the family has lost their form? How do we handle that?

Mr. VIGNONE. That is going to be a little sticky but in essence we are going to require it.

Mr. SIMON. But you are going to accommodate that in some way?

Mr. VIGNONE. Yes.

Mr. SIMON. I read this sentence as I was glancing through your statement here, which at first stunned me. It says, "Forty-four percent of all recipients report erroneous information which affected their award amounts."

At that point I was a little startled and then I read the rest of the sentence, it says, "by plus or minus two dollars or more."

What if we instead of saying $2 or more we made that $100 or more?

Mr. ELMENDORF. Sir, we asked that question ourselves when we got the study. We went to a $150 discrepency and the data we have on that shows that essentially if you have—well, Joe, why don't you provide that?

Mr. VIGNONE. If an error tolerance of $150 were used, then 47 percent of the recipients, and I believe I am reading this right, were paid in error but 41 percent were plus or minus $2.

Mr. SIMON. So something is wrong with your statistics.

Mr. HASTINGS. If I understood your question it would be what percentage of the students are within $100 of the reported income. Is that your question?

Mr. SIMON. No, your statement is 44 percent of all recipients reported erroneous information which affected their reward amounts by plus or minus $2 or more.

Now, I am frankly not worried about a $2 error. I think when we get into $100 or $150 then you are talking about something significant and obviously if you go to $100 or $150, you said it is 47 percent, then something is wrong with the statistical data that you are using.

Mr. **Vignone**. The problem I think is in the way it was presented. The answer to that is that 73 percent of the recipients were paid in error and if you used $150 plus or minus in award error then 47 percent of the recipients would have been in error.

Mr. **Simon**. That still does not add up. If you can send me a clarifying memo I would appreciate it.

[The information follows:]

PELL GRANT AWARD ERROR

When only application error is considered, that is, student reporting error, then 41 percent of students were paid in error within a tolerance of plus or minus $2.00. If a tolerance of plus or minus $150 is adopted, 24.6 percent of recipients were paid in error due to application mistakes.

Mr. **Simon**. Then, on your request for $5 million of program funds made available the continuing resolution being reprogramed to pay for the additional processing costs, I understand you are before the Appropriation subcommittee on that request today?

Mr. **Elmendorf**. Yes, sir.

Mr. **Simon**. I have conveyed to our colleague, Bill Natcher, my concern. I am concerned that we nibble away on it. Five million dollars is not a huge amount in terms of the total program, but if we start using the Pell grant program for administrative costs, where are we going to stop? And I have to say on that basis I am not very enthusiastic about reprograming $5 million. I would be interested in your comment.

Mr. **Elmendorf**. I understand that from the tenor of your questions you would like to get into the validation question immediately so let me see if I can't give you the overview on the study and then get specifically to why we are recommending what we are.

The questions you asked of the Inspector General bother me too because I have not found significant cases of willful abuse in the program. However, we do have from a study that we have conducted for ourselves, as a result of our quality control effort, enough nationally based and significantly determined evidence to assess the fact that there is a great deal of misreporting in the program by students.

Our determination is that if we can correct the misreporting we could, in fact, save $289 million in that net overaward to students. That is a significant dollar finding.

Mr. **Simon**. $289 million?

Mr. **Elmendorf**. $289 million in net overawards to students could be saved. It was our opinion that we had to take the initiative and propose alternatives for savings.

We have made several such proposals. The first was to have the contractor centrally validate applications.

Timeliness was the issue in that case because the processor could not make the necesary changes for 1982-83, if we did not notify them with some degree of accuracy by December 30.

Realizing that that was not going to be possible we chose our second best alternative and one which I personally favor; that was, to return the authority to the institution to verify all the eligible

Pell Grant applications using 1040 data. We would validate only two elements. Two elements were selected because they were the two most critical elements. They are most critical in the sense that they could retrieve for us the greatest amount of funds. The greatest amount of that $289 million could be saved doing the least amount of work by institutions in the field.

And doing that, we estimate the cost to us, exclusive of a per application verification fee of $2 for the institution, to be about $1.9 million. That would involve additional corrections, returns to the contractor from institutions for new data, and telephone inquiries and so on. It is an estimated figure that we feel is justifiable.

At the same time, we felt that the institutions should be compensated to some degree for their work. We estimated that to be about $2 per eligible applicant from which we derived a figure of $5.2 million to be returned to the institutions.

Mr. **Simon**. Is time the problem in asking for that in the supplemental?

Mr. **Elmendorf**. Yes, sir, if we expect to have that system up and running to cover the awards for this year, we will need to have a decision rather soon because we are now waiting to notify institutions that this is the appropriate way to go for this processing year. We would like to effect those savings in this processing year. So, yes, it is a rather critical time question.

Mr. **Simon**. Finally, two questions on NDSL. In a GAO report of September 30, 1981, they report a default rate as of June 30, 1979, of 16.04 percent. The report is dated June 30, 1981. I am a little startled by the lateness of that date. GAO said 1979 is the latest date for which data were available.

I guess my question is really a twofold one. Why doesn't GAO get a more recent date? What does it look like now? Don't we have any better idea?

Mr. **Elmendorf**. It is very close to those numbers. The reason we can't get that data in a more timely fashion is because it is institutionally determined and institutionally submitted data. It comes to us as part of the fiscal application for funds which usually is sent to us around November. That information is now being keypunched and is available.

Mr. Moore is our expert on the NDSL program and is prepared to answer your questions in that area.

Mr. **Moore**. Mr. Simon, the most recent data we have is for academic year 1979-80. The 1980-81 data, as Dr. Elmendorf indicated, is now being moved through the system and will be available later this spring.

The institutional default rate in NDSL as of June of 1980 was 11.9 percent. I want to underline institutional default rate because it is a term that you will see us increasingly using and that means the default rate on paper held by all of the participating colleges and universities.

It is true that the overall default rate in the program is 16 percent. The reduction has come about in two ways. The largest part of it is because institutions have assigned paper over to the Federal Government. We now hold about one-third of a million accounts which are being fed into our collection system.

When those accounts are assigned to us they come off the institution's books and reduce the default rate.

The second is the fact that institutions, through their own efforts with billing and servicing agencies, have cured defaults that they have been holding and that has further reduced the rate.

What we are trying to do right now is to push through new regulations which with our collections effort and our general urging of institutions to take old paper off the shelves should help institutions resolve a default problem that is 15 years in the making; that is, from the sixties and early seventies.

Having been involved with it one way or another since this time in 1960, I have a rather personal feeling for seeing the problem resolve before I eventually retire from Federal service.

I can't retire until we get that default rate down to about 8 percent.

Mr. SIMON. You may be in Federal Government a long time.

Mr. MOORE. We are headed in the right direction and it seems to me that within another year or year and a half we will have the institutional rate down below 10 percent.

Mr. FORD. That makes it about even with the unemployment rate.

Mr. MOORE. There is a certain similarity there. I don't know quite what it means.

Mr. FORD. They are passing each other.

Mr. SIMON. Two other questions, Mr. Moore, if I may direct this to you. The GAO report shows outstanding loans submitted to you of $215 million and collections of $3.8 million. That is not a particularly impressive number.

Mr. MOORE. That is right. And the reason for that is that at the same time we were picking up all of these assigned notes from institutions in 1979 and 1980, we also had mounted a major effort with our portfolio of defaulted FISL paper. That portfolio amounted to half a million loans of a much larger amount.

Both of those default portfolios are in our automated system about which Mr. Hastings can comment in much more detail. We hope to obtain the same recovery on our NDSL portfolio.

NDSL collection actually was a manual process being used at our regional offices which is not nearly as efficient as the contracting system we have now.

Mr. SIMON. And then finally, let me just toss the same question out to you. As I was reading the Inspector General's report, it occurred to me, do we have the right kind of mix in personnel in education policymakers versus people who are watching those dollars very, very carefully, the accountants and so forth?

Mr. MOORE. I would say yes, because if one looks at the sources of our personnel over the last 15 years, we are staffed by people who have come from State agencies, for example, Dave Bayer from New Jersey in the midsixties.

I came from California out of the banking community. We have people from other Government agencies who have worked with credit programs, a lot of the original GSL staff came from FHA with a lot of experience in handling long-term obligations and Government guarantees.

We have a number of people with DP background, with accounting backgrounds. Certainly in our policy organizations we have had people moving in from financial aid slots on campuses.

Now the converse is true. We have a number of very capable young folks saying goodbye and exiting to go and help the same organizations that we got other people from over the years.

Now, I would say with some Irish luck and good hiring practices, we will achieve a fairly decent mix in the agency.

Mr. SIMON. Thank you.

Mr. Ford.

Mr. FORD. How many loan collectors do you have?

Mr. HASTINGS. During 1981, from March when the Secretary ordered us to rely on private collection agency efforts, rather than continuing to do this with total Federal employment, we have gone from about 1,000 down to 288 Federal collectors on board, I believe.

Mr. FORD. I am not talking about the individual. I am talking about the positions you need to meet the Office of Management and Budget's requirement of reduction in the Department and the impression that you absorbed 500 or so slots.

Mr. HASTINGS. I can't speak for what the Secretary did on that. I don't think that that was necessarily the nexus of events.

I can tell you what happened to the SFA staff.

Mr. FORD. When did you get started with the private contractors to collect?

Mr. HASTINGS. The major contracts were awarded 2 months ago and the first day of operations by the private contractors was yesterday, as a matter of fact.

I think what is important to note, however, and this is the point that we have made to the Secretary, is that while we had on board about 800 fewer Federal employees, we collected virtually the same amount of money in fiscal year 1981 as we collected in fiscal year 1980 with many fewer people.

Now, there are several reasons for that. One of them is that we benefited from an annuity because the accounts had already been started in payment and we were reaping the benefits of prior actions. But the fact is that we were able to accomplish several things. One, we consolidated 10 regional offices to 3 with respect to the collections effort.

That entailed confusion with respect to pieces of paper moving back and forth, people being transferred, writing the request for proposals and awarding the collections contract, yet still maintaining those dollars for the taxpayers. The credit for that certainly has to go to the fine people in our regional offices, primarily who were involved in that effort

Mr. FORD. Well, the formal statement indicates on page 15 these contracts will result in average commissions of 29 cents per dollar collected.

Mr. HASTINGS. That's correct.

Mr. FORD. They started business yesterday so we don't know how it is going to work out, obviously. Can one of you explain to me how it is supposed to work at 29 cents on the dollar?

Mr. HASTINGS. Well, the contractors, of course, get nothing if they don't produce, which is the standard practice when we are paying a commission rate. This is unlike the Federal employees, of course, whom we had to pay whether or not they brought in a dollar.

Mr. **Ford**. The Federal employees, last time I looked, were bringing in 2 bucks or something for every buck it cost them.

Mr. **Hastings**. Yes, and an average rate of 25 percent.

Mr. **Ford**. But it is only 29 percent of that which they collected. They get nothing for what they don't collect.

Mr. **Hastings**. I don't understand.

Mr. **Ford**. When they collect the dollar, they get 29 cents instead of nothing, so 29 cents on the dollar doesn't mean a thing to me because if they cream the business and send you back a paper that is hard to collect, you will lose your tail.

You ought to be at least as smart as Montgomery Ward when you pay your bills.

Mr. **Hastings**. If you look at it from a cash flow—I don't think there is anything wrong with creaming from a——

Mr. **Ford**. There is nothing wrong with creaming, provided somebody else has to pick up the tab for what is left. If you were a doctor with a practice out there and you hired a collection agency and they creamed the top off and let the rest of your accounts go, you wouldn't put up with that very long.

Mr. **Hastings**. I see what you are saying.

Mr. **Ford**. What protection do you have?

Mr. **Hastings**. As you may know, we had two-pilot contracts, one in Atlanta and one in San Francisco, which Secretary Califano ordered us to implement. We learned a little bit from that experience.

One of the things we learned was that collection agencies went about this business a little bit differently than we had been doing with respect to the documentation of the paper necessary under the joint standards promulgated by Justice and the GAO.

So when we wrote the RFP, we learned a little bit from that. We required that they can go ahead and cream the paper in the sense that they take the largest accounts first and work them. If they do that and it is successful, we all win because the money will be coming back to the Treasury in the biggest amounts first.

On the other hand, we don't want this paper to be kept by the contractor. The contractor has to give that paper back to us within 15 months if they have not been successful in getting collections started on it.

Yet we don't want to get that back and start the process all over again. The RFP was written with a number of steps required, steps which varied with the dollar amount of the loan. The contractor has to perform certain minimal specified steps on every single piece of paper that they have. Our ultimate desire and our point of view when we wrote the RFP is that if that paper comes back to us, it is either repaid or the person has died, is disabled, he is bankrupt, has been discharged, or the case is right for litigation.

We move it on to whatever is appropriate under the joint standards at that point. That is our desire. Now, whether or not we are going to be successful on that, we don't know.

We do know that we have a lot of people who bid on those proposals. They said they could do that and they signed a contract with us saying that they would do it.

Mr. **Ford.** I am startled at the arguments that you have and I just want—though it sounds really great, what requirement is there that I don't collect the 10 percent of the easiest money and send back the rest and then get a new batch of paper and take 10 percent of that?

How much am I allowed to accumulate in uncollected paper before they will give me more paper to cream? You said you are not bothered with creaming?

Mr. **Hastings.** We have attempted to provide some safeguards in that area. We have onsite monitors in each of the three locations where the contracts are being performed, Chicago, Atlanta, and San Francisco. They will be selectively sampling the paper that is in the hands of the contractors now and will be during the first year of operation.

We will be measuring what is happening to that paper and where dollars are not coming in. The way the contracts are written, contractors are not guaranteed that we will exercise their option to continue their service beyond the first year.

And if it turns out we have a bad contract, we know what to do about that. We can publish the same RFP again and reopen the competition if that is necessary.

Obviously, we don't think that will be necessary. We think we have good, competent folks who know what they are doing in this business and who will perform.

Mr. **Ford.** I am sure the chairman shares my concern that you succeed in this effort because, as you well know, this committee put a great deal of effort into forcing the old Office of Education and subsequently the Department of Education to take the cards out of the shoebox and put things on a computer and start collecting loans. I was shocked to discover, as chairman of this committee, a few years ago, that we had all of this bad publicity about the default rate on guaranteed student loans and nobody in Washington ever asked anybody to pay the bill.

Nobody ever sent a letter and said, by the way, Charlie, do you know you owe us some money. When we finally started sending letters, we discovered it was too late, we didn't know where they lived.

Those people who did get a letter, a surprisingly large amount, just by getting a letter from the Office of Education went into the office and got into repayment status. Then we permitted you to negotiate repayment schedules and to compromise balances like other lending institutions and then last year we gave authority to get the recent addresses from the IRS.

Now all of these things over a period of years were a response to what this committee perceived to be not only the public concern, but our own concern that the integrity of the program which depended on getting that default rate into a realistic frame so that you can understand what the reason was.

Because the implications were that the default rate was extraordinarily high, vis-a-vis other kinds of credit, and that that was because students generally were a nondeserving bunch of creeps left over from the sixties who had been stealing from the system.

We have been fighting against that image for these programs for a long time. I personally feel that the taxpayers out there would be a lot happier in supporting the program if they knew we were doing the very best job possible to collect.

And I am sure that that is what you are trying to do, but we want to make sure we don't get six months or a year down the road and then see that we are under fire on these programs because the previous put-into-place collection system has now been dismantled.

Literally, you just have begun that work over there with the collectors and you have the computers going and now we are going to a whole new way to do it.

I don't want to see a lot of this paper laying in collection agencies' back rooms because they are waiting for you to send them some new stuff. That is easy to collect.

One more question about that worries me a little bit; we are not allowed to share the IRS information agency with the collection agency, are we?

Mr. HASTINGS. I am not an expert on the Privacy Act.

Mr. FORD. It is not a question of the Privacy Act, it is the Internal Revenue Code, which makes the person's income tax return confidential from all sources, absent that exception we made for you?

Mr. HASTINGS. We are doing a tape match with IRS before the paper goes to the collection agency.

Mr. FORD. You keep the information you get from IRS in-house and you give them an address?

Mr. HASTINGS. We send the first bill on it, as I recall the way the process is being done.

Mr. FORD. We don't want somebody coming up with an injunction in the middle of this.

Mr. HASTINGS. Let me provide verification for the record.

Mr. SIMON. Fine, we will enter that into the record.

[The information follows:]

MOST RECENT ADDRESS INFORMATION

The Department of Education submits social security numbers and names of defaulted borrowers to IRS annually in order to secure the student's most recent address. If the social security number matches IRS records, this information is then recorded on the GSL/NDSL data base as best address information.

The loans that are being turned over to the collection contractors have these updated addresses within the individual records and any other address that may be available. The contractors do not have direct access to IRS skip trace. This access is only through the Department.

The information provided by IRS consists of the borrower's current address as indicated in the last applicable tax return. In the past, if we had a correct social security number on the borrower, IRS would provide us with the first four letters of the new name in cases where there had been a name change (borrower married, legal changes, etc.). It is important to note that we no longer receive that name change information and this has restricted us severely.

Mr. HASTINGS. I am glad you raised that issue, because we had the same concerns you raised about making sure that what we are doing is not going to result in any sort of diminution of the efforts already started.

The IRS match has been very successful in the last year. We are getting a very large percentage of new addresses as a result of that additional authority Congress gave us.

Mr. FORD. Thank you very much.

Mr. Chairman, I would like to come back after the other members have had a chance.

Mr. **Simon**. Mr. Bailey?

Mr. **Bailey**. Thank you, Mr. Chairman. I have only one question. Could we have proposals for next year's level of funding from the Department of Education?

Mr. **Elmendorf**. I think those proposals will be to you by February 8, as part of the Department——

Mr. **Bailey**. Why don't you just go ahead and tell us now?

Mr. **Elmendorf**. There may have been changes in the proposals that were submitted by us early in the year. We have not seen what we recommended since it has gone out.

Mr. **Bailey**. I have recently been in Missouri and I have seven institutions of higher learning in my district and they seem to have some sort of premonition. In fact, they have numbers and they wave them in my face.

Now, why don't I know what they are?

Mr. **Elmendorf**. Well, I think the——

Mr. **Bailey**. They have been on the radio talking about what is going to happen, in my district, before I get there. It is all primed and cut for my arrival in Columbia, Mo?

Mr. **Elmendorf**. I would like to have the same numbers. I think that——

Mr. **Bailey**. Would you like for me to have someone call you? [Laughter.]

Mr. **Elmendorf**. I would like to corroborate those numbers with the ones we sent up.

Mr. **Bailey**. I can go down to last year's and they say that is gone, that is zeroed out, this is a billion less, this is 100 million less. You have not seen those?

Mr. **Elmendorf**. I am going to have to wait myself until the 8th of February to see those numbers.

Mr. **Bailey**. Thank you, Mr. Chairman.

Mr. **Simon**. Thank you, Mr. Bailey.

How many institutions participate in the NDSL?

Mr. **Elmendorf**. Approximately 4,000.

Mr. **Simon**. Of that number, how many are over 25 percent in default?

Mr. **Elmendorf**. I think about 800, I am estimating now, probably 800.

Mr. **Simon**. How many are between 10 and 25 percent? Roughly?

Mr. **Elmendorf**. Roughly 900.

Mr. **Simon**. So we have about 2,300 below the 10 percent?

Mr. **Elmendorf**. 1,700 above 10 percent.

Mr. **Simon**. If I am following you, 800 are above 25 percent, 900 are between 10 and 25.

Mr. **Elmendorf**. We have in there, Mr. Chairman, some institutions that are not now receiving Federal capital contributions—A, because they have been denied or, B, because they never requested it in the first place, which is a result of the fact that they realized the default rate is too high and they could not meet the due diligence requirements.

Mr. **Hastings**. Or because they are revolving.

Mr. **Simon**. Can you give me a breakdown, using whatever figure—I am just trying to get a picture.

Mr. **Elmendorf**. Yes, sir, I have got that available in the record.

Mr. **Simon**. Can you just give it to me orally here at this point?

Mr. **Hastings**. If you look at the 3,300 schools that received capital last year, which break did you want to know, Mr. Simon?

Mr. **Simon**. Just very rough?

Mr. **Hastings**. In 0 to 10 percent, 45 percent of the institutions had less than 10 percent. That is about 1,500 schools, 1,484.

Mr. **Ford**. You qualified it. Are you only giving us those institutions who received additional capital last year?

Mr. **Hastings**. These 3,200 schools represent schools that received capital last year.

Mr. **Ford**. As distinguished from a school that has a successful program where they have a revolving fund now? Why don't you throw the successful ones in the pot?

Mr. **Hastings**. Because our program's operations folks have the numbers on who they gave capital to last year.

Mr. **Ford**. That doesn't make sense. You talk in your statement here about ones that have their own program, the ones where it is working the way that idealistically we expected it to work in 1965, and those are not covered because it is working.

Mr. **Hastings**. I am not sure for what purpose Mr. Simon is asking this question. If he is asking this question to determine the impact of the new regulation on schools, I think these are the ones he wants to know about.

Mr. **Simon**. I want to get an overall picture of where we are. I gather from your response to my colleague's question that we are—and from your earlier response, you are dropping both those who are successful and those who are massively unsuccessful who have not reapplied. Is that correct, or is that not correct?

Mr. **Hastings**. The figure I just read you is based on the experience of the 3,266 schools that got capital contribution last year. That is the way the computer spit it out.

Mr. **Ford**. So maybe it averages out that a school is really bad and can't qualify, didn't ask for money and the schools that are doing well didn't ask for additional capital.

You don't know what that means in terms of the percentages on this.

Mr. **Simon**. I would be interested if you could submit those figures for the record, including the schools, the 800 you do not include and why they, you know, are not included.

Mr. **Elmendorf**. Could we answer that question from the point of view that you need to know or would like to know the type of institutions that are affected by the new regulations, those with default records over 10 and those with default records over 25?

Would that be satisfactory?

Mr. **Simon**. That would be.

Mr. **Elmendorf**. I will give you that data now: 782 schools with default rates over 10 percent; 800 schools with default rates over 25 percent. The breakdown, roughly, in the over-25-percent category is nearly 58 percent proprietary institutions, 19 percent 2-year public, about 4 percent 2-year private, roughly 8 percent 4-year public, and 13 percent 4-year private.

Mr. **Simon**. And that is on a base of how many? Is that 3,200, then?

Mr. **Elmendorf**. Yes, I believe it is.

Mr. **Ford**. Are those percentages based on number of institutions without regard to size, or based on dollar volume for your program?

Mr. **Elmendorf**. I believe that is number of institutions throughout.

Mr. **Ford**. So we can't assume from that that 55 percent of the bad money out there is coming from proprietary schools?

Mr. **Elmendorf**. No; I can't make that assumption.

Mr. **Ford**. They are generally pretty small, aren't they?

Mr. **Elmendorf**. Yes.

Mr. **Ford**. Can you punch another key over there and tell us a dollar volume of the bad money we are talking about, where it is?

Mr. **Hastings**. I am pretty sure we can, sir.

Mr. **Simon**. Then, finally, the GAO made seven specific recommendations. Of those seven specific recommendations, where do we stand upon their recommendations?

Mr. **Elmendorf**. In which program, sir? NDSL?

Mr. **Simon**. Yes.

Mr. **Hastings**. I think we will have to provide that for the record.

Mr. **Elmendorf**. Mr. Moore will have to respond to that, but he has had to take a call from his secretary.

[The information follows:]

RESPONSE TO GAO RECOMMENDATIONS

GAO recommendation.—Require school to comply with the Department's loan servicing and collection procedures, particularly with respect to bringing suit against defaulted borrowers and submitting defaulted loans more quickly to collection agencies

Action taken to date.—The Department is in the process of tightening its program review effort in the area of NDSL billing, collection and litigation to more specifically pinpoint areas of non-compliance which require corrective action.

GAO recommendation.—Require schools to monitor results of collection agencies' actions.

Action taken to date.—An article is being prepared for the OSFA bulletin, which is distributed to all institutions participating in the NDSL program.

GAO recommendation.—Establish limits for the time a loan remains with an agency for collection.

Action taken to date.—A Notice of Proposed Rulemaking (NPRM) has been drafted incorporating a six-month limit on the amount of time a collection agency may work and NDSL account. This NPRM is currently in the first stage of clearance.

GAO recommendation.—Establish an acceptable default rate and suspend from the program or withhold Federal funds from those schools that exceed the establishd default rate.

Action taken to date.—An NPRM was published on January 7, 1982, on the NDSL. CWS, and SEOG funding procedures. A provision was included in the NDSL portion of the NPRM providing that institutions with default rates above 25 percent will not be entitled to any new Federal funds. In addition, any institution with a default rate between 10 and 25 percent will have a penalty applied against the amount of Federal funds it will receive. The public comment period ended February 25 and the final regulation is currently in clearance.

GAO recommendation.—Determine whether submissions of National Direct Student Loans to the Department for collection earlier than the statutory two year time limit would be beneficial to collection efforts and, if so, consider proposing legislation to allow schools to submit defaulted loans as soon as possible after completion of required collection activities.

Action taken to date.—An amendment to the statute has been drafted and is now in final clearance. The amendment will be included with other proposed amendments in a legislative package which will be forwarded to Congress.

GAO recommendation.—Propose legislation to allow credit bureaus to redisclose student loan data referred to them if the Department's review shows that such redisclosure is presently restricted by law. Should the Department's review find that present law does not restrict credit bureaus from redisclosing student loan default data, the Secretary should advise schools and credit bureaus of this matter.

Action taken to date.—We have pulbished an article in the August/September issue of OSFA *Bulletin.*

GAO recommendation.—Assess the economic feasibility of its plan to use private collection agencies to insure that their use is the most cost effective means of collection defaulted student loans. Any reassessment should consider the potential of agency wide application of the collection program presently in place in one region that is returning approximately $6 for every $1 spent.

Action taken to date.—The Department did not concur with the recommendation.

Mr. **Simon**. Mr. Ford

Mr. **Ford**. I am fascinated with these new regulations. How do you clear these with the fellow at the White House who counts the pages of regulations for the President's speech record? I have never seen a Chief Executive that can rattle off the number of pages of regulations.

I have been here 18 years and it absolutely awes me when I hear those people down there, as if you could measure the effectiveness and value of programs by the number of regulations.

Here you are describing those regulations that you feel are absolutely essential to restore honesty, integrity, and all of the good things to the program. How many more regulations have you got in the pot at the moment which we are going to have to consider this year?

How many pages are you going to take up in the Federal Register this year with regulations from this excess agency called the Department of Education?

Mr. **Elmendorf**. The answer to that question, if there is an answer to that question, is that there will be as few regulations as possible but those that are, be developed, we hope will be under the rubric of self-regulation, self-regulatory standards of satisfactory progress. These are being developed right now but need clearance as a response to the GAO report on satisfactory progress.

Others will be regulations we feel can improve the management of programs and can be of some benefit to institutions and students. I see the reduction of the default rate in the NDSL program as a long-term benefit to new students who have not yet begun higher education by contributing to the revenues of those funds, which are not now there.

So we have to answer that question. If it promotes good management and self-regulation, we hope to put out more of them.

Mr. **Ford**. Now you just said the magic words and I remember what was bothering me about what our former colleague, the under secretary, said in the Appropriations Committee and what was repeated today about the mandatory requirement that a student applicant furnish the family's income tax return.

Why can't we rely, as we have up until now, on the same kind of self-regulation and simply be satisfied with the affidavit-type application that says: My dad told me he made $25,000 last year?

Why, with this concern against overregulating and deep concern that the Federal Government is in everybody's pocket, peeking in their bedroom, are we talking now for the first time in a long time of telling every family out there that has children going to school that you have to submit to each of the schools they are going to the family's income tax return?

I think that is a terribly deep intrusion into the privacy of the family and I don't think it relates to the obligation of the family to support the child's efforts to go to school?

Mr. **Elmendorf**. I would be in your court on that. Information should first be self-reported and accurate. Our findings from our studies show that as much as we would like to trust the accuracy of that information, it is, in fact, not accurate.

Mr. **Ford**. The main problem with the accuracy has nothing to do with the honesty and integrity of the person making the information. You ask a child at the beginning of the year to tell you what is going to be on the tax return in April, and then maybe the father gets called back to work or something has happened the kid doesn't know about, and what they said in September and what actually shows up on the tax return is something different.

You know, there is no evidence again that we were able to find when we looked at this and really rejected the idea of putting families through this, as a matter of fact, the orthodox conservative line for years was that the middle-class Americans couldn't get a student loan without going over too many hurdles, too many hoops, and answering too many personal questions about their life that the Government had no damn business asking.

Now here we are, after all of these years of moving away from that, suddenly now coming back to the most intimate document the Federal Government forces people to file.

We already intruded on the privacy of that filing last year when we gave the Office of Education the special exemption that lets you find somebody by seeing where they are paying their income tax. That was, to me, at the time, a matter of some concern and I raise it again today.

But now you are asking to put in the hands of every employee in a public or private institution a copy of the return.

Why wouldn't a form that contained the necessary information repeating what is on the tax return, limited to those numbers that you really need, signed by the student as his commitment of what the return shows, do the trick?

Mr. **Elmendorf**. I think that, in fact, is what the program application is now. It is a statement including data from records and a certification that the information is accurate.

Mr. **Ford**. But you don't have to attach a copy of daddy's tax return to the Pell Grant application at the present time?

I understand you will mandate that?

Mr. **Elmendorf**. We are proposing that that application for 1982-83 be processed without the 1040, because there simply isn't time to do that.

When it is sent back to the institution, the student is directed to send a 1040 directly to the professional student aid officer where it is attached to the application and the information is verified. The eligibility index, to avoid delays on behalf of the student getting his money. Advance payments would be given to the student so he would not be prohibited from enrolling.

That kind of system, to me, doesn't seem to restrict the system. Rather, it allows us to say that data we had is accurate and the student is not being prohibited from joining the program on a less-than-honest basis.

That is my major concern with the program. Too many people are getting awards that are, in fact, $300 million in excess of what they should be.

That bothers me and I think we have a responsibility at the program office to propose a solution. Now this may not be in your mind the best solution, but after considered thought, it is the best one we could come up with at this point.

Mr. FORD. But the essence of your solution smacks of the suggestion that there is a deliberate attempt to mislead or misrepresent the facts. And somebody else here said that it usually happens because they don't know; they really don't know.

Now, that is not going to be helped by filing the family tax return. But I will tell you what is going to happen, if you want to save some money in the budget, this is one of the ways to do it.

We wrestled with this problem for a long time because several years ago we had major lending institutions—we had a real problem of availability of guaranteed student loans. So we started really trying to find out why are there parts of the country where people won't and types of communities where banks won't get into the student loan business?

We found the single most important complaint that banks had was that we made them force the family to bring in a tax return and verify a family income as a condition precedent to the eligibility for the loan.

And the loan application was not enough. And banks were using that argument wholesale across the country as an excuse for not handling that loan and making it available to kids.

I am afraid that the anxiety of the ordinary citizen who used to believe that the one thing he filed with the Government that was secret between him and God and his Government was his income tax return. Now we not only are going to get information from it if his kid doesn't pay his loan, but we are going to have the whole thing on file someplace where it is no longer protected by the sanctity of the rules of the IRS.

Now, having said that, I am indicating to you that the last alternative, if there is anyone else available, that I want is something that provides that kind of a threat to privacy that inhibits the willingness of the parent to cooperate with the child in securing the loan.

Suppose the father made $10,000 as a bookie or a numbers runner last year. If he is smart, he is going to pay his income tax on it, but he doesn't want to tell everybody else in the world that is how he is making his income.

That seems to me to be something you ought to try to avoid, and I am not so sure with a little bit of thought that we couldn't—just a little bit of trust, not too much, but we might be able to come up with an affidavit-type application that gave you the numbers that you need and not the details.

Mr. **Elmendorf**. Sir, I would be more than willing to have that kind of system if I thought it would work. My problem is that I am sitting here with the Pell grant application in my right hand which requires the parent and student both to certify to this statement: "All of the information on this form is true and complete to the best of my knowledge. If asked by an authorized official, I agree to give proof of information that I have given on this form. I realize this proof may include a copy of my 1981 U.S. State and local income tax."

They realize, also, that if they do not provide proof, the student may not get in.

Mr. **Ford**. That is if you catch somebody you think has lied to you, they have in advance agreed and I don't even like that part of the procedure, but they have agreed, if it becomes essential to look at the family income tax return, we will bring it in, look it over together.

They have not agreed in there to file a copy of their return up at one of our huge factories student aid offices with thousands of part-time students having access to it and God knows what is embarrassing to the family on it.

I don't think that I want to file a tax return as a congressman and everybody see who I owe money to.

Mr. **Elmendorf**. 300,000 of those parents and students now do submit their 1040's because they are identified for validation by us and they are required to submit those forms directly to the institution. The institution gives a very thorough analysis of all the elements on the form to find out if there is fraud or abuse. That is 10 percent of the total applicants.

Mr. **Ford**. Does a person walk in and say, here, I will prove to you I am correct, take a look at my tax return, at least you will know if I lied, I lied the same way to Uncle Sam as I have to you.

That is one thing. But having a person, as the condition precedent to processing the paper, file and put into the permanent possession of an institution the family's 1040 seems to me to be quite different.

It has been permissible to ask for that information and even ask to see it in the past. It is not something that we just sort of did by accident. Over the years, this has been argued back and forth.

I wish Mr. Ashbrook was here. He is for some a guaranteed orthodox conservative who I know agrees with me on this and he would let you know this is not a liberal/conservative concern of this committee, but one of long standing.

Maybe we could work out an alternative to that.

Mr. **Elmendorf**. I think I understand your point.

Mr. **Hastings**. I would point out that the proposal we presented to Congress would not reveal to whom you owed money. We were only asking for page 1 and 2, which do not have the deductions, for instance, don't have schedules A and B and all of the rest of the attachments.

Mr. **Ford**. A very alert person in the audience just asked me, how do you know that the copy of the tax return is legitimate?

Mr. **Elmendorf**. We don't.

Mr. FORD. You don't know what I filed with Uncle Sam. I can show you what I made out and then my wife refused to sign it because I was cheating by 5,000 bucks so I made out a different one.

You really are asking——

Mr. SIMON. Are we relating history of yourself now, Mr. Ford? [Laughter.]

Mr. FORD. That doesn't give you the integrity or security you are asking for, but subjects the honest, overwhelming majority of the American people who want to participate in the program to a whole lot of redtape, if you will, and bureaucratic intrusion in their private lives.

The payoff is not very good. If I want to cheat by lying under oath on an application for a student aid, do you think I would hesitate to bring you a phony copy of a 1040? No; if I am going to go that far, I have already committed the felony, why not get another 6 months and make it look good.

What you would get filed with these people, a copy of the return, you couldn't get a copy returned from IRS, this verifies that the taxpayer paid their tax according to this return this year.

You would get the carbon copy that H. & R. Block gave them when they had their tax made up. And most of them would be honest.

But the very person you are trying to catch would have certainly the imagination to realize how easy it is to get—go down to the post office, get an extra 1040 and make out a phony.

Mr. HASTINGS. To turn around the statement you made a minute ago. The problem we are attempting to address here is not that category of people who are going to lie to us a second time. We want to get the tax returns from the people who are giving us the honest returns, who have made, in most cases, an honest mistake on their application originally.

That will be corrected.

Mr. FORD. Why don't you ask them for specified relevant information from the return, rather than the filing of the return? That is the whole point. Ask me what my adjusted gross income was and ask how much I paid in State and local income taxes—that is now a factor, isn't it?

And all of the relevant facts that I have disclosed on my return, let me put that on an application and sign my name. Don't ask me to ask my father to put his tax return on file at Podunk State College.

Mr. ELMENDORF. That is what we are asking for and getting right now on this application form, by everyone, signed by student and parent.

That is the reason we have reached the conclusion we have. Because I would rather go this way, and believe that self-reported information is accurate. Our study shows it is not, in 44 percent of the cases.

And the difference between the 44 percent and the 71 percent error rate is the institutional error rate and we could talk about that if you wish at some later time, perhaps now.

But we are saying 44 percent of the students are making errors. I don't think they are intending to make errors, but they are making errors on their application forms, significant enough to cause $289 million in over award.

And the low-income students, at least the trend that we get from the data we looked at, is that the lower the income of the student, the greater they list their income to be. They, in fact, have under awards.

The converse of that is true as well. Higher income students understate their income and therefore, we have an over-award situation. It is quite significant.

Mr. **Ford**. Have you, in formulating this regulation, talked to the people in the student financial aid business?

Mr. **Elmendorf**. We have been working with the National Association of Financial Aid Administrators, Dallas Martin, before Christmas, sent a questionnaire——

Mr. **Ford**. He agreed to this regulation?

Mr. **Elmendorf**. I am sure he will agree with it. He has not gone on record as agreeing to it, but——

Mr. **Ford**. I bet he wouldn't want you to tell me if he did. On the serious side, I feel I may be overly sensitive to this, but I would like to know what some of those old pros around town in this business for so many years feel the impact will be?

Are we buying a whole bunch of additional problems for the schools? Are we cluttering up the whole process here? What is the payoff?

Is it likely to produce enough to make the effort worth while?

Mr. **Simon**. If my colleague would yield, I think this is also why we also ought to have the breakdown of not $2 or more, but much more substantial amounts. We need an idea of what kind of abuse we are talking about and what may be necessary to correct that.

Mr. **Elmendorf**. I might say we are proceeding in collaboration with the National Association of Student Financial Aid Administrators. They are collecting information to the extent to which this data is already being collected, in some cases it is being collected on a statewide basis for all students attending, in States like California.

Perhaps 2 years ago I would have had the same feeling as you. It is a different environment now. More people are supporting this because they, I think, feel they are protecting their own funds out there.

Their funds are scarce and they are trying to allocate them the best way possible. They are using the 1040, and not just the front page, but all of the schedules attached, to sort out who should receive the aid, not only for Federal aid, but institutional aid, scholarships, grants, assistanceships.

My concern also is like yours, when you get information as sensitive as a 1040 or as an application for admission which has some very personal information on it.

How do you treat that? Under the Buckley amendment, which in my institution we followed, was that information held by professionals in files and not abused and misused in the institution.

I would consider the 1040 to be in the same category. It is that kind of protection that I think institutions can afford and would afford to this system.

Mr. **Simon**. Mr. Bailey?

Mr. **Bailey**. Thank you, Mr. Chairman. I don't find your analysis of the 1040 unreasonable.

Thank you, Mr. Chairman.

Mr. **Simon**. You have no further figures from Columbia, Mo., for us?

Mr. **Bailey**. No, but I wonder if someone in the room might not know. Perhaps it is Congressman Ford's friends at the back of the room.

Mr. **Ford**. I think you are being discriminated against as a member of the minority party.

Mr. **Bailey**. Thank you, Mr. Chairman.

Mr. **Simon**. We will submitting some additional questions to you for the record, we appreciate your being here today, we look forward to working with you.

The subcommittee will resume hearings tomorrow morning at 9:30 in this room.

[Whereupon, at 4:30 p.m., the subcommittee was adjourned, to reconvene at 9:30 a.m., Thursday, January 28, 1982.]

OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

THURSDAY, JANUARY 28, 1982

House of Representatives,
Subcommittee on Postsecondary Education,
Committee on Education and Labor,
Washington, D.C.

The subcommittee met, pursuant to call, at 9:35 a.m., in room 2257, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Weiss, and Erdahl.

Staff present: William Blakey, majority counsel; John Dean, minority counsel; and Maryln McAdam, legislative assistant.

Mr. Simon. The Subcommittee on Postsecondary Education today continues its oversight hearings on the Federal student assistance programs. We are pleased to welcome several distinguished representatives of the higher education community who will provide their perspective and responses to several important issues.

Jack Peltason, former chancellor of the University of Illinois, will lead off our panel today. I want to commend each of the organizations and you gentlemen individually for spearheading a response from the higher education community on the subject of "satisfactory academic progress" of students receiving Federal student aid. The response of the community is not only important to students and the institutions, but to the integrity of the programs themselves. Senator Pell, in particular, along with me and others on the subcommittee have been concerned about the "quality" issues in postsecondary education.

As the subcommittee elicited from witnesses at yesterday's hearing, one cannot believe everything you read or hear about student aid abuses. Today's testimony is an excellent example of the responsiveness of the college and university community to congressional concerns.

Also today, we will have the concerns of institutional administrators and of students about the processing problems in our Federal student aid programs.

Our panel consists of Dr. Peltason, president of the American Council on Education, Douglas Conner, executive director, American Association of Collegiate Registrars and Admissions Officers, and a frequent visitor to our subcommittee, Dallas Martin, executive director of the National Association of Student Financial Aid Administrators. I am very pleased to have the three of you here.

Dr. Peltason, we will start with you. For these witnesses and any other witnesses today, we will proceed as you wish. We can enter your statements in the record. Summarize them or however you want to proceed.

STATEMENT OF JACK PELTASON, PRESIDENT, AMERICAN COUNCIL ON EDUCATION

Mr. Peltason. Thank you very much. I am pleased to be here. I will enter my statement in the record, and rather than summarize it, supplement it and make a few comments. I want to assure you and your colleagues that we have a longstanding tradition of self-regulation in the higher education community, but we have been accelerating our efforts in the last several years in that direction, because we are as anxious as anybody to reduce to a minimum the abuses in the programs of student financial assistance.

We think the most effective way to do that is to get the community sensitive to the problems, to adopt guidelines and enforce and implement them, working closely with our colleagues in the Department of Education rather than to try and enforce inflexible single national standards on the 12 million students in the 3,000 educational institutions of the United States.

I can report that we have had considerable success. We have had an Office of Self-Regulation since 1978 working with the other education associations. We have now promulgated the self-regulation guidelines. Copies of these are available to the members of the committee. And let me just mention some of them and show you how I think they serve as a model.

We have had a problem for some time, for example, in the area of tuition refunds. The student loan program calls for a tuition refund statement. It has been the contention of those of us in higher education that there should not be a single refund policy for each and every institution in the United States. There is too much diversity out there. However, we do accept the notion that if you participate in a program you have an obligation to have a refund statement, and you should publish it and make it available. So working with the Department of Education we developed guidelines, and distributed them widely. We have had workshops. Our guidelines have been adopted as the official regulations of the Department of Education.

We feel the same approach will be effective, the most effective single way to deal with the problem of reasonable progress toward a degree. We worked on that problem for some time preceding the recent publicity that has been given about some abuses, and I want to make it clear that we in no way defend those abuses and are anxious to do all we can to stop them. We think they are not widespread, but we acknowledge that some exist.

Our approach has been to develop guidelines working closely with our colleagues from the Department of Education. Those guidelines have been developed. We accelerated our effort after talking with Congressman Simon I believe a year or so ago when the question came up, I think, during the discussion of reorganization legislation as to whether or not we should put in a Federal standard.

I assured the Congressman that with reasonable time we would give top priority to developing guidelines. They have been developed; 10,000 copies of them have been distributed. Workshops are now being held around the country as those responsible for the implementation of this program are being informed about them.

Copies of those guidelines are again available to you. They essentially say that every institution must have a policy. It must have a policy that applies across the board. It must have an appeals procedure, and every institution must evaluate each student at least once a year to insure that they are in compliance. It does not try to spell out in any mechanical way precisely how to measure reasonable or satisfactory progress.

Let me conclude by saying that having been a dean of a college, I know how difficult it is to develop a standard. You can be committed to the notion of being tough and holding to the standard, but you still have to have some discretion to deal with the so many different kinds of situations that develop.

I remember from my experience at Illinois we had a rule that you had up to I think the eighth week of a semester to drop a class. After that you could not drop a class. You were then committed to it, and if you did not do well you failed.

It is very easy to state that rule, but there were always exceptions. On the beginning of the ninth week of class somebody who had some personal tragedy in the family or with some particular reason, with the application of good sense and judgment without minimizing the standards some compassion and discretion should be given, or otherwise that student might be forever doomed to not being able to complete the degree. So that discretion I think has to be left at that level.

At the same time you have to insure that those who take Federal dollars and administer these programs do so fully conscious of the responsibility to see that the dollars are spent for the purpose Congress intended, and we think we are well launched on that effort.

I will be glad to answer additional questions, but I think it might be more helpful to turn to my colleagues who are heads of the associations most immediately responsible for the development of these guidelines. But I emphasize we work with all the educational associations. They have the expertise, they have developed details, we have discussed them, they have been widely commented on, and they have the actual support of the whole association of education.

[The prepared statement of J. W. Peltason follows:]

Prepared Statement of J. W. Peltason, President, American Council on Education

Mr. Chairman and members of the subcommittee, I am pleased to have this opportunity to speak with you today about actions of the higher education community on standards of satisfactory progress for students receiving federal financial assistance. I have already sent copies of the Joint Statement on Satisfactory Progress to every member of this subcommittee but I would also wish to insert a copy in the hearing record at this time.

I would like to describe briefly our process of self-regulation and to outline the steps we have taken to address problems regarding campus policies on satisfactory progress. My colleagues, representing the American Association of Collegiate Registrars and Admissions Officers and the National Association of Student Financial Aid Administrators, will offer specific comments on the GAO report and on our own approach for improving campus policies on satisfactory progress.

We first became aware of problems with satisfactory progress requirements several years ago and, in 1980, following the debate on this subject during passage of the 1980 Amendments, we moved forward with a self-regulatory approach to their resolution. These actions are part of a larger program of self-regulation to which the higher education community committed itself in 1978. We agreed then that—rather than risk further federal involvement in areas which are the rightful responsibility of the higher education community—we would work systematically to strengthen our own ability to address problems subject to public concern. To do this effectively, we have had to mobilize the resources of a good many education associations, to call on the volunteer time and expertise of individual campus administrators, and to enlist the active cooperation of college presidents in dealing with a wide variety of problems.

Our approach has three key components:

1. to develop and distribute national policy statements of recommended practice;
2. to work together jointly as associations to alert campus administrators to the issues and to the need for prompt campus implementation of the national policy recommendations; and
3. to ask the pertinent association or associations to assume leadership for further follow-up actions on the subject. Follow-up actions may include advisory publications and workshops, consulting assistance, development of model policies, or other actions designed to achieve full institutional cooperation with the national effort.

This is an ambitious and serious undertaking, particularly in view of higher education's diversity and its long traditions of campus autonomy. I'm proud to say, however, that we have made substantial progress with this effort and have gained wide support among our constituent institutions. To date, we have issued Self-Regulation Guidelines on seven topics and have issued longer reports on several other topics. One of our earlier self-regulation statements—on fair and equitable tuition refund policies—was eventually recognized by the Education Department as an appropriate means of compliance with GSL requirements on tuition refund. Our recognition of the importance of proper campus management of student aid led to the publication of both a technical manual and shorter guide on management of student aid. Other self-regulation actions have dealt with college policies on student recruitment and admissions, collegiate athletics, and the confidentiality of faculty tenure decisions. New statements are presently being developed to address concerns in such areas as foreign student recruiting, ethical practices in college advertising, and privacy of employee records.

On satisfactory progress, we completed the development of a national policy statement last October. It was developed in close consultation with the Department of Education. We understand that the Education Department fully supports these community-developed standards and will recognize them as a basis for institutional compliance with the Department's requirement in situations where state laws or accrediting requirements do not already apply. We are now in the midst of a major information campaign to foster immediate campus action to review and improve policies on satisfactory progress. By joint actions among education associations, more than 10,000 copies of the statement have been issued. Recipients include the presidents of all U.S. colleges and universities, as well as registrars, business officers, student affairs officers, academic vice-presidents, and financial aid officers. We have also called it to the attention of accrediting agencies and have asked them to take it into account as they review campus policies and procedures.

Two additional actions add further impetus to our campaign: the National Association of Student Financial Aid Administrators (NASFAA) has just completed preparation of a monograph that offers sample policies and detailed explanations of points covered in the national policy statement. Further, ACE together with NASFAA and AACRAO have already sponsored a day-long workshop designed to answer questions of individual institutions on their policies for satisfactory progress.

These actions represent a voluntary community response to problems that we have recognized in this area. In this instance, I believe that we have been able to move forward effectively to correct problems that have come to light, yet in a manner that supports local institutional autonomy to the greatest degree possible.

Mr. SIMON. I would like to enter the guidelines in the record, because we may be referring to them as we move along in addition to the formal statements.

[The information referred to follows:]

[From the American Council on Education, December 1981]

SELF-REGULATION INITIATIVES: GUIDELINES FOR COLLEGES AND UNIVERSITIES

JOINT STATEMENT ON STANDARDS OF SATISFACTORY ACADEMIC PROGRESS TO MAINTAIN FINANCIAL AID ELIGIBILITY

The Education Amendments of 1976 required that institutions limit federal financial aid to those students who, according to institutional standards, were in good standing and making satisfactory progress. A 1978 study of the management of federal financial aid programs by the General Accounting Office took serious exception to the paucity of such standards and to evidence of institutional nonadherence even when standards did exist.

Senator Pell (D.-R.I.), who held hearings on the subject of satisfactory academic progress during the development of the 1980 Education Amendments, proposed a requirement that students successfully complete at least 75 percent of their initial academic load per term or period. Although he was persuaded not to insist on so stringent a requirement, the intent of Congress clearly was to give the education community an opportunity to develop effective self-regulatory standards. The need for such standards has increased with the recent removal of the limit on years of eligibility for receiving Pell and SEOG awards.

The American Association of Collegiate Registrars and Admissions Officers and the National Association of Student Financial Aid Administrators have proposed the following guidelines to assist institutions in developing their own standards of satisfactory academic progress to maintain federal financial aid eligibility. In doing so, institutions should consider the relation between these standards and other institutional policies regarding academic progress.

A. Each institution should take all necessary steps to fulfill the federal requirement to implement and make public the standards for satisfactory academic progress that students must meet to be eligible to receive federal financial aid.

The statement of institutional policy on satisfactory academic progress for purposes of continued aid eligibility should be available to all requesting it and should be made public through readily available institutional publications. Each federal financial aid recipient should be provided with a copy of the institutional statement of satisfactory academic progress.

B. In establishing standards of satisfactory academic progress, each institution should respond to the diversity of its students and academic programs. Within a given category and program, such standards should be applied consistently to all students receiving federal financial aid.

Each institution shoud establish standards in accordance with the diversity of its students, for instance, to recognize differences in eductional objective and between full-time and part-time status. Once established, such standards should be uniformly applied to all students receiving federal financial aid within a given category. For example, all full-time students in a given institution and program should be expected to maintain the same minimum academic progress.

C. Each institution should establish and announce a reasonable length of time for students receiving federal financial aid to complete their educational objectives. This time should be consistent with the academic goal of the student and would vary according to enrollment status. The institution's policy on standards of academic progress should include a statement of the effect on academic progress and financial aid eligibility of course incompletion, course withdrawal, course repetition, and noncredit remedial courses.

Institutions should establish limits on the amount of time allowed for students in different enrollment categories (e.g., full-time, half-time) to complete their objectives to be eligible to receive federal financial aid. The time established should include any additional time needed to complete noncredit remedial courses. The institution's policy should clearly describe the effect on satisfactory progress of course incompletion, course withdrawals, and course repetition. A given institution may decide to impose a limit on the number of course incompletions, course withdrawals, and course repetitions. Clock-hour institutions should establish a maximum number of clock hours of instruction for students to complete their programs.

D. Procedures for appeal and reinstatement of aid should be part of each institution's policy on satisfactory progress and should be readily available in writing to all students receiving federal financial aid. When an institution denies aid, reviews a case, or reinstates a student who was previously considered not to be making satisfactory progress, documentation to justify the action must be maintained.

Institutional policy should clearly describe the procedures for appeal and reinstatement, possibly including the conditions under which an appeal may be sought and the procedures by which students may satisfy the deficiencies that led to ineligibility.

E. Evaluation of a student's academic standing and progress to determine federal financial aid eligibility should be made before each award period, but no less often than once per year.

Although some institutions are able to make a formal evaluation of a student's progress after each academic term, many other institutions, due to processing and time constraints, are not able to do so. If an institution can complete formal evaluations only once per year, an effort should be made to conduct more frequent evaluation/monitoring during the year. This will be particularly important in situations involving a probation/warning status or with appeals and reinstatement.

Mr. SIMON. Mr. Conner.

STATEMENT OF J. DOUGLAS CONNER, EXECUTIVE DIRECTOR, AMERICAN ASSOCIATION OF COLLEGIATE REGISTRARS AND ADMISSIONS OFFICERS

Mr. CONNER. Thank you, Mr. Chairman.

I am going to try to follow my text a little more explicitly than Dr. Peltason did, because I am going to try to comment on the GAO report specifically in terms of at least some of the misconceptions that that report may have developed. Our association has a long history of cooperation with a good many of the agencies, particularly those included in the report, and we feel that self-regulation is the best way to address these problems. As I comment on the report I want to assure the committee that in no way do we intend to be defensive, or that my association and the higher education community in general have any desire other than cooperating with any and all Federal officials to see that institutions strive to insure that Federal aid dollars are used appropriately to properly enhance students' educational goals.

For this reason, my comments will concentrate on GAO's recommendation that the Congress authorize the Department of Education to issue regulations setting forth general requirements for institutions to follow in establishing academic progress standards. The self-regulation initiative prepared by the American Association of Collegiate Registrars and Admissions Officers and the National Association of Student Financial Aid Administrators and approved by the American Council on Education provides a framework to accomplish this recommendation without the specifics that are included as part of the GAO recommendations. In my view, cooperative voluntary efforts between the Government and higher education seem to be the most effective way of accomplishing this basic objective.

May I now amplify this and also offer some specific comments on the report that will illustrate that basic point.

As I read the report I had to remind myself in terms of the context of the report that it was an auditor's perception of what satisfactory progress would be, that is in this case an overall "C" average, for three separate Federal programs which have different objectives and requirements.

First, as acknowledged in the report there are no satisfactory progress standards for social security students except that they carry a full-time load by the institution's definition. In 1979, AACRAO and social security worked out a voluntary (nonreimbursed) certification plan that saved the Government $75 million in fiscal 1980. This illustrates, I believe, the very best in terms of voluntary cooperation between the Government and the private sector.

Second, the VA has very rigid standards on progress, nonpunitive grades, changes of program, and full-time status that are not only supported by regulation but often are in the law itself. The VA had 20 lawsuits before Public Law 94-502 was amended, and it seems to many of us who worked on that effort unlikely that anyone would want to repeat a comparable experience of cementing standards into law and regulations. Again, voluntary cooperation such as the AACRAO/social security certification process, the ACE/AACRAO/NASFAA self-regulation initiative on satisfactory progress, and ACE/National Association of College and University Business Officers' self-regulation initiative on tuition refund policies would appear a much better option.

I would like to give you a few more interpretations in terms of points of the study that I think will be helpful toward this overall aim.

The General Accounting Office admits in the report they did not survey any institutions that were selective in their admissions process. The 20 they did review included many with open-door admissions and those institutions did provide flexibility in terms of academic probation, suspension, and so forth, to provide reasonable opportunities for students to succeed. In fact, many selective institutions are flexible in not applying the "C" average requirement in the freshman year. Some of these institutions then also permit such programs as academic bankruptcy, and so forth, and may not require an overall "C" average to graduate. Institutions sometimes compute a separate graduation average that usually requires a "C" average on all work that applies to the degree. This enables a student not to be penalized for "F's" if he/she passes the course when repeating it. Consequently, the overall "C" average standard as applied by the auditors is not necessarily a good or fair measure.

Since the 1960's, institutions developed very liberal course-drop policies, nontraditional grading, and so forth, allowing students to drop without penalty, sometimes up to the day of final exams. This trend is reversing itself now, but open-door admissions institutions may still not have completely revised their policies on dropping courses.

Last, and I guess this is kind of in the picky, picky vein, I have seen a lot of references in the press about coed jogging and advanced weight training. I was interested in terms of the bottom line as far as that student was concerned because the student referenced did graduate. So it is my assumption that those courses in some way applied toward the degree requirements. I say that just in passing because I was interested in how quickly some of the media picked up that fact.

There is also a statement in the report that VA payments are made directly to the student, and that is not completely true. The VA in the seventies asked higher education institutions in a cooperative vein to participate in advanced pay programs and to deliver checks up to 2 months of advanced pay to the veterans upon their registration.

This process was a factor, perhaps a major factor, in the VA overpayment problems in recent years. The premise is that the student is responsible for meeting the necessary requirements of Federal aid. Students sign onto this on their Federal financial aid and on the VA eligibility forms. Institutions report enrollment, withdrawals, terminations, and so forth, but they use their own academic standards to monitor students. We think the system can work this way with the cooperation that now exists between the Department of Education and the higher education community.

Thank you.

Mr. SIMON. Thank you.

[The prepared statement of J. Douglas Conner follows:]

PREPARED STATEMENT OF DR. J. DOUGLAS CONNER, EXECUTIVE DIRECTOR, AMERICAN ASSOCIATION OF COLLEGIATE REGISTRARS AND ADMISSIONS OFFICERS

The association which I represent, the American Association of Collegiate Registrars and Admissions Officers, is a national, non-profit educational association which is composed of membership of over 2,200 accredited postsecondary institutions. These institutions are represented by more than 7,200 individual staff members from the fields of recruitment, admissions, registration and records, student financial aid, and institutional research at the undergraduate, graduate, and professional levels.

Traditionally, our association has had a close and rewarding working relationship with federal agencies concerned with higher education. This has been particularly true in terms of the Social Security Administration, the Veterans Administration, and the Department of Education. Through mutual understanding and cooperation, for example, we have been able to bring institutional collegiate staff members in to Washington to work on ad hoc committees with these agencies in order to provide implementation advice on the respective laws with the users' expertise.

We've been invited to comment on the GAO report and I would like to offer remarks in that regard, emphasizing to the committee that in no way do I want to make it clear that the comments are defensive or that my association and the higher education community in general have any desire other than cooperating with any and all federal officials to see that institutions strive to ensure that federal aid dollars are used appropriately to properly enhance students' educational goals.

For this reason, my comments will concentrate on GAO's recommendation that the Congress authorize the Department of Education to issue regulations setting forth general requirements for institutions to follow in establishing academic progress standards. The self-regulation initiative prepared by the American Association of Collegiate Registrars and Admissions Officers and the National Association of Student Financial Aid Administrators and approved by the American Council on Education provides a framework to accomplish this recommendation without the specifics that are included as part of the GAO recommendations. In my view, cooperative voluntary efforts between the government and higher education seem to be the most effective way of accomplishing this basic objective.

May I now amplify this and also offer some specific comments on the report that will illustrate that basic point:

A common standard was applied in terms of an auditor's concept of what satisfactory progress is (an overall "C" average) for three separate federal programs, with different objectives and requirements

(1) As acknowledged in the report there are no satisfactory progress standards for social security students except that they carry a full-time load by the institution's definition. In 1979, AACRAO and Social Security worked out a voluntary (non-reimbursed) certification plan that saved the government $75 million in fiscal 1980. This illustrates, I believe, the very best in terms of voluntary cooperation between the government and the private sector.

(2) The V.A. have very rigid standards on progress, non-punitive grades, changes of program, and full-time status that are not only supported by regulation but often are in the law itself. The V.A. had 20 lawsuits before Public Law 94-502 was amended and it seems to many of us who worked on that effort unlikely to me that anyone would want to repeat a comparable experience of cementing standards into law and regulations. Again, voluntary cooperation such as the AACRAO Social Security Certification process, the ACE/AACRAO/NASFAA self-regulation initiative on satisfac-

tory progress, and ACE/National Association of College and University Business Officers' self-regulation initiative on tuition refund policies would appear a much better option.

A further interpretation on points of the study:

GAO admittedly did not survey any institutions that were selective in their admissions process. Many open door admissions institutions provide flexibility in terms of academic probation, suspension, etc., to provide reasonable opportunities for students to succeed. In fact, many selective institutions are flexible in not applying the "C" average requirement in the freshman year. Some of these institutions then also permit such programs as academic bankruptcy, etc., an may not require an overall "C" average to graduate. The Institutions sometimes compute a separate graduation average that usually requires a "C" average on all work that applies to the degree. This enables a student not to be penalized for '"F's" if he/she passes the course when repeating it. Consequently, for overall "C" average standard as applied by the auditors is not necessarily a good or fair measure.

Since the 1960's, institutions developed very liberal course drop policies, allowing students to drop without penalty, sometimes up to the day of final exams. This trend is reversing itself now, but open door admissions institutions may still not have completely revised their policies on dropping courses.

Lastly, in the picky, picky vein, the co-ed jogging and advanced weight training courses; the bottom line is that the student did graduate. Those courses must have been used as elective hours or the physical education requirement.

The statement in the report that V.A. payments are made directly to the student is not completely true. the V.A., in the 1970's, asked higher education institutions to participate in advanced pay programs and deliver checks (up to two months of advanced pay) to veterans upon registration. This process was a major factor in the V.A.'s overpayment problems in recent years. The premise that exists in the V.A. regulations and in Department of Education programs is that the student is responsible for meeting the necessary requirements of federal aid. Students sign on to this on their federal financial aid forms and on V.A. eligibility forms. Institutions report enrollments, withdrawals, terminations, but use their own academic standards to monitor students. The system can work with the cooperation that now exists between the Department of Education and the higher education community.

APPENDIX I

DEPARTMENT OF HEALTH ADMINISTRATION,
SOCIAL SECURITY ADMINISTRATION
Baltimore, Md., March 17, 1981.

Mr. J. DOUGLAS CONNER,
Executive Association of Collegiate Registrars and Admissions Officers, Washington, D.C.

DEAR MR. CONNER: As you are aware, over the last two years the Social Security Administration (SSA), with the cooperation of your organization, has initiated significant changes in the student benefits enforcement operation. While all of these changes have not been implemented as smoothly as you or I would have hoped for, nevertheless, data available to me indicates the changes have resulted in significant improvements in our program. For example, we estimate that the verification requirements, in which your organization plays such a vital part, helped us avoid making over $75 million in incorrect payments during fiscal year 1980. On behalf of SSA I would like to thank you, your staff in Washington, and the thousands of members of your organization who have assisted in our efforts to make the student benefit enforcement program more effective.

Sincerely yours,

SANDY CRANK,
Associate Commissioner
for Operational Policy and Procedures.

Mr. SIMON. Mr. Martin.

STATEMENT OF DALLAS MARTIN, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS, ACCOMPANIED BY JEAN MILLER

Mr. MARTIN. Thank you, Mr. Chairman. We appreciate the opportunity to be here today and to discuss the area of satisfactory academic progress with you.

You have heard from my colleagues. Dr. Peltason talked about the joint efforts of the higher education community, and Mr. Conner talking about the development of the American Association of Collegiate Registrars and Admissions Officers and our efforts to develop the statement which is in the record. I think that the course that we have launched ourselves upon today in terms of the joint efforts of the postsecondary education community in developing the self-regulation initiatives is very important, and I think Dr. Peltason pointed that out.

You recall, Mr. Chairman, that you along with some of your colleagues, Mr. Ashbrook, Brademas, Ford, and Buchanan on the committee discussed this issue at length during the development of the Education Amendments of 1980. It was a contention at that time that rather than writing specific language into the law, that the reference in the law be a broad statement thereby providing flexibility to institutions to develop those standards that would be the most appropriate for their institution. And so it is in that vein that we have enjoyed working with the other people in trying to develop a statement that is worthwhile that we think can work. I think this is even more important today when we look at the growth and the complexity of the student aid programs and realize that there are so many variances out there that we have some standards and guidelines that institutions can follow. In that regard we began work on this issue some time ago. It was our title IV committee that accepted the challenge to begin to develop specific recommendations. As we began that approach and working through that statement we worked closely with our colleagues at AACRAO, because there is a close coordination with the monitoring and control with the registrars along with the financial community of an institution.

We have developed a joint statement of standards which was accepted by the American Council on Education and other organizations in October of 1981. I think we should also make it clear that it was not just the community that was involved, but people from the Department of Education and other places were consulted and advised and were given copies of the draft for their input as we proceeded.

We are pleased today to say that we have developed the statement, but really it is only the beginning of the effort that the community is undertaking. While we have a statement now that I think makes a lot of sense and provides flexibility, the next thing is to assist institutions in implementing that policy.

We are in the final stages of completing other efforts that we have been involved in for the past few months. One is the development of a comprehensive monograph which we have been working on that will provide specific step-by-step recommendations along with a checklist and some models of other schools that have developed good standards to use with our institutions. That will be published and will be delivered to all the institutions across the country in the next couple of months. We are in the final stages of editing that document, and as soon as it is final, I will be happy to provide a copy of it for your review.

That monograph will be useful as a guide in trying to develop policies. This is critical because in developing such a policy at an institution, we are not only talking about the impact and the use of Federal student aid funds, but getting into some of the basic principles of postsecondary education, the goal of admission and academic programs at institutions. So the policy requires close coordination between not only the financial aid office and the registrar, but more importantly, will involve the president, probably representatives from the faculty and academic vice presidents and many others, because the policy will impact on the recruitment, retention, class size, and other things.

We are excited about the development and the efforts to have the publication done, and once we have the publication completed, we will undertake other activities. For example, the American Council on Education in cooperation with AACRAO and NASFA conducted a workshop in New Jersey where we invited college presidents, financial adminstrators, financial officers, to help develop their policies as a workshop. Another workshop is going to be scheduled in the next month.

Additionally through our State and regional associations, we have sent out a letter asking them to provide a forum at those State and regional meetings where this issue can be discussed and information exchanged between other institutions of how they are progressing with them. We think we will be able through that to have in place an adopted policy that has been designed and fitted to each institution, but we will be able to share the experiences that we have had and try to get more uniformity across the country. In that regard, I think it proves once more that the self-regulation initiative that has been undertaken can work. It is indeed our hope that we can continue in this effort with the Department of Education and with other Federal agencies to allow the postsecondary education community to be self-regulating.

I must point out another thing about the study done by the GAO, and I think Mr. Conner is correct. We do not want to sound picky on the study, but I would be remiss if I did not provide for the record that I know some institutions we visited during the study were engaged at the time in a review of what was going on and had changed a part of their policies substantially. They had a news release coming out about a number of students at that institution that they had dismissed because they were not doing this, and they had really cleaned up their act. Unfortunately, the time frame the study was conducted under looked at data in the files the prior year. There were people that had not taken the responsibility seriously, and therefore it appeared to be in worse shape than it was. That has been changed at that institution along with the others.

At this point I would like to stop and give you a chance to ask questions, and also just to say that I have somewhat oversubscribed myself today and have another commitment. I have a colleague here, Mrs. Jean Miller, who is a former president of our association, who works in an open-door community college that has been actively involved with us and if there are questions I am sure she could assist as well.

Mr. SIMON. Let me play the devil's advocate for a moment and say to the Department, there are people in the Department who will say self-regulation sounds great, it simply has not worked. And they will say these guidelines are fine, what about schools that do not accept the guidelines, No. 1, and No. 2, what if we have a school with a 30-percent default rate, can we just ignore that? What is your response?

Mr. PELTASON. I think a school that fails to properly police its own house, that does not have an effective program to insure that reasonable progress is made toward a degree, that some action should be taken against that school to say that you are not carrying out your responsibility. We do not believe that self-regulation means that the Federal officials have no responsibility to insure that the law is complied with. It provides a standard for them to implement and enforce.

Mr. MARTIN. One other thing that I think will assist the Department of Education is that we have been working with the national regional accrediting associations for postsecondary education getting them to subscribe to this and to make certain that institutions we are accrediting develop such policies. It is my understanding from talking to people in the Department of Education that when they issue the regulations that they plan to specify that this will be a part of it, and then for those few institutions—and there are very few not covered under accrediting agencies—they plan to reprint those as the guidelines that you should follow. When they are doing compliance, if they discover that an institution is not adhering to those policies, they no have a basis to write that up as an exception. I think we will find quickly that the vast majority of institutions will adopt these and will police themselves very well.

Mr. PELTASON. It is my understanding that the Department will make these guidelines part of its regulations.

Mr. SIMON. Do either Mr. Dean or Mr. Blakey have any questions?

Mr. DEAN. In the 1980 amendment Senator Pell's recommendation that 75 percent of the initial courseload had to be satisfactorily completed, what arguments could you make that we should not adopt that now to kind of address the problems in the GAO report?

Mr. MARTIN. I would like to comment and perhaps my colleagues would like to say something about that. I think the main concern that the community had with an arbitrariness of the 75 percent is that not all institutions, when you begin to look at various systems of judging academic performance, would adhere to that. For example, there are academic programs out there that are lab kinds of courses, particularly in medical areas or nursing, where a student will engage in that course, and it is really a pass/fail. You either complete that and develop the expertise and skills necessary out of that, or you are required to repeat that.

Under a stiff requirement that is arbitrary, there is no way to assess that. In this case the student might be dropped out altogether, when in fact maybe all they needed was additional work for 2 or 3 weeks to complete part of that and they would do it. It was primarily in that vein that we expressed our concern about the arbitrariness of having in the law the 75 percent. In actuality, many schools may have standards higher than that. So our concern was the grading policies.

Perhaps Dr. Conner would like to comment on that, since he is much more familiar with those procedures than I am.

Mr. **Conner**. I think we have a general concern about overlegislating requirements, as I suggested, or standards into the law. If you will look in the GAO report and the VA's response to that report and see the scenario of problems they have had with doing that in terms of law itself, they have had to amend those laws, and in fact when we looked at Vice President Bush's initiative in terms of reducing regulations, we found that we could not make a lot of comments on some of the VA programs because the requirements were in the law, not in the regulations. I think that is my big concern, and the fact that we think the self-initiative process as demonstrated, for example, through the social security program, will be much more effective.

Mr. **Peltason**. The difference between a university regulation and a Federal law is significant. I would not object to that kind of regulation if a university chose it, but I would insist that there be some human being to apply some discretion to take care of the case where there is not abuse, where you are standing in the way of some student's progress because of some special circumstances.

You cannot waive a Federal requirement. That is the difficulty. But again from my own experience, it is not an uncommon thing for a student to start off his or her academic program in the wrong field. Maybe they started in the college of engineering because their father wants them to be an engineer, and they do not do well there. You have to apply some judgment. Maybe if that student transferred to another college there is a course of study he or she could complete. If you have a rigid requirement saying if you flunk so many courses that is it, you cannot exercise that discretion. We do not want an institution that has no standards, but the Federal law imposing inflexibility across 12 million different students, each of whose course of study requires some individual attention.

Mr. **Dean**. Has anybody looked into effect that an academic—say that Senator Pell's standard was enacted, has anybody looked into what effect that would have on some schools that are struggling now and they could lose a substantial number of students? Say we put in a rate-of-progress provision and the nonpunitive-grade provision and a grade-progress provision. Would some schools be jeopardized, or would we see the professors being instructed to give them all "C-pluses"?

Mr. **Peltason**. I have not myself looked nor do I know of studies that looked at the consequences of that either in terms of—I think there would be a general attempt to comply, but again I think as you suggest, there are other problems—75 percent of what? If people did want to cheat, there would be ways to cheat even on that kind of standard, cheat in the sense that they were allowing the students to stay in school only to get Federal funds rather than to be making some progress toward some educational goal.

Mr. **Weiss**. Let me ask, and Mr. Martin may know the answer to this. Is there any data existing as to what standards exist in the community of various institutions? Is that going to be in your monograph?

Mr. **Martin**. We will provide models of several of those that we have collected. They have not attempted to survey to make certain that every institution has one, but I would say that for a number of years we also have another publication that the association has used, and it is actually accepted by the Federal auditing agency, which is our institutional self-evaluation checklist. In that document it also goes through as one of the items that you must have in compliance and talks about the development of a policy, institutional policy of satisfactory academic progress standards. We are going to build on that and try to expand that checklist with additional items to make certain that the various points covered in the guidelines will be included so we make certain that every institution can make certain that their policies are adhering to the standards that have been developed.

Mr. **Conner**. The self-regulation suggests an institution should publish those policies in their bulletins, catalogs, or brochures. In anticipation of this hearing I went through about 50 catalogs to see if there was some statement on academic progress or probation. I found each institution's catalog that I checked had fairly specific statements in terms of academic probation on satisfactory progress and so forth. That is certainly not a sufficient sample. It is more institutions than the GAO study included.

Mr. **Dean**. One concern that has been expressed to me a number of times is that a number of institutions had economic and racial de facto segregation before the 1960's, and what they have done now is set up a preferential admissions policy for these students. Many of those schools now have flunkout rates that are pretty much zero, and they will not flunk out anybody even if the grading is blind. In many institutions examinations are graded by a randomly selected number. Given that that is the fact in many institutions, and disagree if you do not think that is the case—but I am under the impression that at many institutions, including those with selective admissions processes, that there is in fact nobody flunking out of those schools.

Mr. **Martin**. One distinction that needs to be made, if we may, and I am certain I would agree that that is true at a lot of schools—I think there are a lot of schools adhering to standards, and there are students admitted under special programs that may not succeed. One of the lines that we tried carefully to draw here that I think is the concern in terms of the taxpayer and in terms of our role as custodians of public funds, is we were not attempting to tell an institution what its academic standards or policies might be. If we are going to use public tax dollars to provide financial support to students that may not have the financial means to obtain that education, that at some point if that student is not working reasonably toward completion of a degree under judgments that we have invested quite a bit here and by this time he ought to be through, the goal was to say you may still be allowed to stay in the institution, but you are not going to be eligible to receive public funds any longer. The purpose of the student aid programs is to provide assistance to students to obtain postsecondary education. It is not an income maintenance program to sustain people for the rest of their lives. The distinction we wanted to draw is that the student aid funds are there to obtain an education. At a reasonable point, if the student is not doing that, the public tax dollars that we are responsible for cease.

Mr. PELTASON. I would also elaborate, we also want to leave some room for the institutions to adopt a variety of different approaches to education. We have some very highly selective admissions schools that have as a policy rigid standards for admission, but once admitted they generally tend to be rather generous about the length of time it takes the students to obtain their degree. They have counsel and so on. And their approach is we will admit only the academically talented and we will work with them and get them a degree. We have other schools with open admission and their approach is we will give everybody a chance the first year, and they are rather coldblooded about flunking them out quickly. We have all kinds of distinctions in between.

The statement here is that that is the only approach to solve that problem. We do not believe that the Federal Government has an obligation to perpetually support people as professional students. At the same time we do not want to cut down opportunities for institutions—it poses a question as to whether 4 or 5 years is normal. The fact is a good many very good students today may be working, may have other kinds of part-time obligations. If you must start, you must take 14 hours, must also make a "C" and you have to complete in 4 years and you do not, there is something wrong—I think that is an overly rigid specification.

Mr. DEAN. I can appreciate that. In this self-regulation effort, what percent of the students do you see actually being determined to be ineligible for aid as a result of that? In reading this document I can easily see some schools would promulgate regulations and enforce them very strictly and everybody would still be eligible for aid. I think that is likely to happen unless the Department sets more rigid standards. Do you see a lot of students being made ineligible, or just a few?

Mr. MARTIN. I certainly do not have any concrete data to substantiate what the numbers might be. I can tell you from discussing the matter with my colleagues at the institutions that I know that a number of them following your standards review those once or twice during the year in terms of progress of the student, and when students are found that they are not doing that, they are removed. Mrs. Miller has just shared with me here that in her institution at Pasadena City College in California, she has noted that under the guidelines, 5 percent of the students would be disqualified annually at her institution with the guidelines that you have. She says that is her procedure. Can she expand on that?

Mr. DEAN. Do you think these students will wind up dropping out of school as a result of no aid?

Mrs. MILLER. Yes.

Mr. DEAN. So you will lose them altogether?

Mrs. MILLER. We will lose them at that time. However, many of them get religion and return at a later time, another semester or another year.

Mr. **Dean**. And if we left them eligible for aid, do you think a lot of them would straighten out in another term, or do you think it helps them when they see the sword over their head?

Mrs. **Miller**. I think we would find at an open-door institution, if they did not have standards, they would take advantage of the system.

Mr. **Dean**. Thank you, Mr. Chairman.

Mr. **Simon**. Let me make a comment in line with Mr. Dean's question here. I think one of the concerns of one of my colleagues who were in the other body, one that I share, is that we have to pay some attention to this whole quality problem and that there is a danger, particularly as we cut funding and as we lose students that schools are going to be moving in the wrong direction, and I think there are at least several of us who have some concerns in this direction.

Mr. **Martin**. Mr. Simon, I might just add though while I think that has been a suspicion, there has been a lot of evidence recently that many, many institutions are actually tightening up on their standards that are getting more and more selective on admissions policies. There have been some major universities recently that have announced tightening of policies. Ohio State is one, Florida is another, that are going to tighten up on this, just the opposite of what we would assume during a period of tightening funds and reduced enrollments.

Mr. **Peltason**. Miami Dade Community College is, also. I think you are right, the apprehension that you express is one that some of us have, the fear that in a time of shortage of students people might engage in recruiting. We also have some self-regulatory guidelines having to do with ethical advertising, with recruitment. We are now working over those relating to recruitment of foreign students, because I think everybody in the higher education community does not want to see us go through a period in which we lose the public confidence by abusive practices or engaging in things that we consider improper. I think that danger is real, but I think we are alert to it. There will always be some who will violate those standards, but by having the standards it will be readily identified, and then if punitive action needs to be taken, it will be against those institutions rather than adopting a regulation constraining those who do behave.

Mr. **Simon**. I was not suggesting that the grade point average was a way to solve this problem. I am aware of what Harvard and Stanford and Ohio State; I was not aware of the Miami Dade action. I am not sure the examples cited are necessarily going to be typical of what is going to happen in the higher education community. I hope maybe they are.

Mrs. **Miller**. I think—I was going to say earlier, before you even asked the question, that I would have less concern about satisfactory progress guidelines with the shortage of funds, because I believe that most institutions will tighten up their standards as what we call a fund-rationing device. It is one way of using fewer funds for the students that you have. And it may mean a loss of some students.

Mr. **Peltason**. In the fifties it well might have been if we had more students, that would bring more resources to your institution, but that is not necessarily going to be the case today. If you have fewer dollars, you want to make sure you are spending them on those students that are most promising.

Mr. **SIMON**. Mr. Erdahl.

Mr. **ERDAHL**. I have no questions, but thank you. I have looked the material over quickly.

On second thought, I guess I will ask one question. Perhaps this is one you should be directing at us rather than any one of us to you, and of Mr. Peltason. On the third page you mentioned that the "On satisfactory progress, we completed the development of a national policy statement last October. It was developed in close consultation with the Department of Education. We understand that the Education Department fully supports these community-developed standards . . ." and so forth. Where might this commitment be if we see modifications in the U.S. Department of Education, or to whom will they be shifted?

Mr. **SIMON**. Answer this carefully.

Mr. **ERDAHL**. If I am ever invited down to the White House, I will ask the same question, but I will ask you, since you are here.

Mr. **PELTASON**. I assume that there will be somebody responsible for enforcing these particular regulations, wherever he is located in the Federal structure. If you ask my guess as to what the ladies and gentlemen of the Congress are going to do, my suspicion is that there will probably still be a Department of Education for some time.

Mr. **ERDAHL**. I just talked to a group of intelligent young people from the Close-Up Foundation and I coined a new initial definition of PPP. One of them asked what that stood for. I said PPP stands for the force in Washington, personal Presidential persuasion. I guess I would take issue if the President decided to abolish the Department, as he said in his recent speech. I suppose he would be successful in the Congress in accomplishing that. I hope we will see these programs carried on in a satisfactory manner someplace else, though I am dubious that that can be accomplished.

Thank you, Mr. Chairman.

Mr. **SIMON**. Mr. Weiss?

Mr. **WEISS**. Thank you, Mr. Chairman. I have no questions.

Mr. **SIMON**. We thank the three of you for your testimony. We look forward to working with you.

Mr. **SIMON**. Mr. William Ihlanfeldt, vice president for institutional relations of Northwestern University.

STATEMENT OF WILLIAM IHLANFELDT, CHAIRMAN, FEDERATION OF INDEPENDENT ILLINOIS COLLEGES AND UNIVERSITIES, AND VICE PRESIDENT FOR INSTITUTIONAL RELATIONS, NORTHWESTERN UNIVERSITY

Mr. **IHLANFELDT**. Mr. Chairman, I welcome this opportunity and I come here not as vice president for institutional relations at Northwestern, which is a rather innocuous or amorphic title and includes such areas as admissions, financial aid, registrar, government relations, et cetera, but I am here today as the chairman of the Federation of Independent Illinois Colleges and Universities, which represents 52 different institutions in the State. I happen to be one of three representatives to that organization that is not a president.

I have been asked to address the question of the financial aid calendar and the processing of the Pell grant program, and I welcome this opportunity. I have submitted testimony for the record, and I will simply supplement that testimony.

Mr. **Simon**. Your statement will be entered in the record.

Mr. **Ihlanfeldt**. The financial calendar, from our perspective, has been untimely and has minimized the impact of billions of dollars of Federal funds. I do not wish to negate the significance of the Pell grant program, but I simply do not think it has realized its full potential.

In 1977 two ideas merged. One idea was to simplify the financial aid process, and that was under the capstone multiple data entry, with the idea that students would file a single application for receipt or eligibility of all types of funds, Federal, State, and institutional.

The other idea was a concern of the Department of Education, and that was how could they better monitor abuse in the program or fraud in the program. What emerged out of those two ideas was an agreement that applications for Federal funds, particularly the Pell grant program, could not be submitted until after January 1, and there must be particular line item reference from the IRS forms to the financial aid form.

Also a part of that was the fact that the major contractors in the country wanted to be a part of this system, and therefore moved their dates forward so that all applications allegedly would be completed after January 1 or after the W-2 forms had been received. Families attempted to complete the IRS forms and then extracted information from IRS to the financial aid form keeping in mind that the reason for this requirement was to address the concern of abuse and fraud.

Now, in the admissions business, and I have been a part of that business for 17 years, from our perspective the issue is that the earlier people have information the better choices they can make, and frankly, no matter how much one makes an effort to communicate that people are eligible for funds, until they actually receive a chip or a voucher which says you have the funds, they cannot plan. Frankly, they do not work very well in a world of uncertainty.

Now, there were many alternatives suggested at the time this decision was made in 1977, and one of those was that families could submit information on the basis of estimated income. Awards could be made during the fall of the year, and verification documents could be sent to these families or the recipients after April 15. My financial aid staff tells me that would include six items.

What has happened to the system or what has the financial calendar wrought? Has it been simplified? For some of the major States and for the Federal Government it possibly has been simplified, but in recognition that this would mean a lack of planning and would encumber the admission processes of many schools, the schools have spent record amounts of funds to try to penetrate many markets that I think have been disenfranchised to some extent by this program. We now have in fact more applications in the environment than we had in 1977. Many of those are institutional.

Has abuse been decreased? Is there less fraud in the system which was the principal reason for tying it to the IRS statement? I think I address this in terms of some data that I cite in my statement, but the behavior of the Department of Education suggests that they are not satisfied with the system as it is, because they do require verification of campus financial aid offers and have asked for verification of 100 percent on the campus. The reason why they have tied this to the IRS statement does not seem to exist any longer.

Has the number of applications been reduced by various marketing segments? I think NASFA studies, studies more recently by Howard University, would suggest that it has impacted as but one example in the black community in terms of increasing mobility.

Has this affected the college on broader horizons? I think I answered that question. I think the lateness of the system simply does not permit broader horizons.

Let me give you an example. What has happened in the higher education system is that students go through the process of trying to make a decision of where they should go to school, and after they have made the decision they find out that they are either eligible or ineligible for funds. If that system was moved forward by 6 months and they knew they were eligible, I think you would find a different behavior pattern with respect to where students would elect to go to school and their own commitment to education during the senior year. If you are told that you have $1,800 or $3,000 or more available to you upon completion of your high school degree, I think you will perform differently than if you find that out in August after you have graduated from high school.

What are the options available to change this system? I recognize that there are all kinds of study committees, but that is part of the problem. I do not think there would be any difficulty in moving that calendar forward 6 months if Congress could make decisions quicker in terms of taxes on income.

How could we validate the system? The Pennsylvania Higher Education Assistance Authority has now demonstrated as did the Illinois Scholarship Commission, that prior year data is a better index in terms of accuracy and in terms of making sure there is less fraud and abuse. If that is not acceptable or if that cannot work, we can always go back to the idea of estimated income with a followup in the spring of the year. And the followup document would go directly to the subcontractors, who would then verify it and move it onto the major contractors.

The irony of this, it strikes me as ironic, is that we are investing billions of dollars in this program over time and several billion a year, a couple billion at least, but when we get to the processing question and say should we in fact have this kind of verification in April, we are told it is too costly, that a million bucks is too costly in order to make sure that we are maximizing individual opportunity when the expenditures exceed several billion. Now specific early information would fulfill the prophecy of the program and the goals of the Senator for the program which bears his name. It would expand opportunities, reduce some of the inequities between social classes, and also optimize the use of Federal funds.

Thank you.

[The prepared statement of William Ihlanfeldt follows:]

Prepared Statement of William Ihlanfeldt, Chairman, Federation of Independent Illinois Colleges and Universities

The issue that I have been asked to address today is the Federal Financial Aid Calendar. From the perspective of the member institutions in the Federation of Independent Illinois Colleges and Universities, the current processing of student financial assistance is untimely, limits individual educational opportunity, and minimizes the impact that billions of dollars in federal student assistance should have upon reducing social class inequities through the Pell Grant Program. The problem is the lateness of the processing schedule, which is caused by the explicit requirement that, before a family can qualify for assistance through the Pell Program, specific line item information must be extracted from the Internal Revenue Service Form and placed on the Financial Aid Form. The earliest that such information is available to most families is in the first week of February upon the receipt of the W-2 Form(s). Moreover, most families do not complete their Internal Revenue Service Forms until March and April. Bureaucratic and processing problems often cause further delays. Thus, families are inhibited in their college planning, for it is common for students not to receive an announcement of their award until near or after they have graduated from secondary school. By this time, the vast majority of students have already decided where they intend to pursue their educaiton beyond secondary school. As a result, the current Calendar, instead of broadening individual horizons and educational opportunities—the hope of the Senator whose name the program bears—limits the effect of the Pell Grant Program mainly to providing access at the local level.

The aforementioned application requirement was imposed by the Office of Education in 1977 with the intent of limiting fraud and abuse. Alternatives to achieve the same purposes, without undermining the original objectives of the program, were suggested at that time. However, these other options were rejected and the focus was placed upon curbing fraud and abuse rather than expanding educational opportunity. Since that time the data suggest that abuse has not been remedied, that there is a more accurate methodology than utilizing the base year income information and related line item Income Tax Form referencing, and that black enrollments—as but one index of program impact—have either leveled off or decreased at many four-year public and private colleges and universities.

Fraud and abuse.—The Department of Education, apparently now less confident of reducing abuse through delayed processing and line item referencing with tax forms, has increased its vigil by requiring the campus financial aid offices to validate reported income information on a random sample of recipients through the collection of Internal Revenue Service Forms. Moreover, a recent proposal has been generated by the Department of Education to validate adjusted gross income and other items for all recipients through the campus financial aid officer—a burden that could not be easily accommodated. In other words, the very reason for the existence of the current processing schedule no longer is valid.

Methodology.—Currently, knowledge of 1981 income data is required, as reported on specific line items of the 1981 Internal Revenue Service Forms, before a family can complete a financial aid application. This is known as the base year. A recent study by the Pennsylvania Higher Education Assistance Authority found that prior year data, or in this instance, 1980 income, adjusted for inflation, is a more accurate measure of determining family financial need. A similar result was found by the Illinois State Scholarship Commission in the early 1970s. These findings invalidate any claim that the processing of financial aid applications ought to be delayed in order to require the inclusion of base year income. In other words, the Calendar should be moved forward.

Impact.—Periodically, the question must be asked of any program, "Is it achieving its original purposes?" The Pell Grant Program was created to increase access to postsecondary education and to expand educational choice. The answer with regard to access is, "possibly", with regard to choice, "doubtfully, at best".

Studies by Astin,[1] Gladieux[2] and the Institute for the Study of Education Policy[3] have presented the following findings: (1) that 33 percent of all freshmen had not heard of the Pell Program; (2) that from 1977 to 1979 there was a dramatic decrease both in Pell Grant applications and in full-time freshmen enrollment among all dependent students from families with real incomes under $12,000; (3) that the percentage of black students not receiving Pell Grants at predominantly black colleges increased by at least ten points from 1977 to 1979; and (4) that black enrollments either leveled off or decreased at four-year colleges and universities during the latter half of the 1970s. As members of the Committee well know, these reported changes occurred during a period when the amount of student aid was reaching its zenith.

A SIMPLE SOLUTION

In order to provide students with the fullest opportunity to achieve their educational objectives as well as to accommodate Congressional concerns about fraud and abuse, I recommend a procedure that would move the Financial Aid Calendar substantially forward, with the intent of achieving the dual objectives of expanding educational opportunity and minimizing fraud and abuse. As suggested above, prior year data adjusted for inflation provide a more accurate index than base year data in determining a family's ability to pay for higher education. This fact permits the acceleration of the Financial Aid Calendar and allows more time to validate information. Validation of prior year data could be continued on a randomly selected basis through the campus financial aid office.

Should base year income information be required, in addition to prior year, such information could be collected through a subcontractor after April 15. Should cost be a factor, it is recommended that the student recipient pay a nominal fee for the processing of the second document. For example, a family would be able to complete the Financial Aid Form as early as the summer between a student's junior and senior year in high school based upon prior year data. Awards could be announced as early as October 1, which would substantially facilitate a student's educational planning. If base year information were also required, a subcontractor could collect such information in the spring of the student recipient's senior year in high school. Should the reported base year information deviate less than 5 or 10 percent from the adjusted prior year information the award would remain the same. Deviations in incomes that were greater than 5 or 10 percent would possibly require a change in the award. This validation procedure, if necessary, would permit a national system of verification without third-party institutional involvement. Subcontractors would not transmit any information to the major contractor until the system had been updated or until a specific date. Except for a limited number of cases, there would only be one transfer of data from any one subcontractor to the major contractor.

These comments are not intended to minimize the significance of the Pell Grant Program, because, clearly, its impact upon the educational system has been substantial; yet, only with a change in the Financial Aid Calendar can the original objectives of the program be realized: that of expanding educational opportunity and reducing the inherent inequities between social classes. Moreover, an earlier processing schedule would not only permit better family planning but would provide the federal and state governments with more time to validate information, thus, reducing fraud and abuse while increasing the impact and breadth of the program.

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[1] Astin, A. W. and others, *The American Freshman: National Norms For Fall 1977*, Laboratory for Research in Higher Education, Graduate School of Education, University of California, Los Angeles.

Astin, A. W. and others, *The American Freshman: National Norms For Fall 1979*, Laboratory for Research in Higher Education, Graduate School of Education, University of California, Los Angeles.

Astin, A. W. and others, *The American Freshman: National Norms For Fall 1980*, Laboratory for Research in Higher Education, Graduate School of Education, University of California, Los Angeles.

[2] Gladieux, L. and Byce, C., "As Middle-Income Student Aid Expands, Are Low-Income Students Losing Out?" a report for presentation at the 8th Annual Conference of the Southeastern Association of Educational Opportunity Program Personnel, Jackson, Miss., Mar. 4, 1980 (revised July 1980).

[3] Institute for the Study of Educational Policy, "Equal Educational Opportunity Scoreboard: The Status of Black Americans in Higher Education, 1970–1979," Institute for the Study of Educational Policy, Howard University, Washington, D.C.

Mr. **Simon**. Thank you. Do I understand your suggestion, what you are suggesting is that in October you can apply or use the 1980 basis? Then sometime after April 15 there would be a verification document or a document that could modify that if it went over 5 or 10 percent; is that correct?

Mr. **Ihlanfeldt**. I think there are two ways to approach this. One is use the prior data and then simply have a sampling on the campus, or you could use the prior year with a verification after April 15. The alternative would be estimated income on the base year rather than the prior year, with a verification document after April 15. Because the concern that the Office of Education expressed in 1977 was that they would reduce abuse by tying the application process to the IRS document, that seems to be no longer valid because they do not use it anyway.

Mr. **Simon**. I was interested in your statement on page 3, I have to say I was not aware of this before, that 33 percent of all freshmen had not heard of the Pell program. Is that the Pell program identified as the Pell program——

Mr. **Ihlanfeldt**. It is referred to in NASFA's questionnaire of roughly 500 colleges and universities across the country. The question is have you heard of the basic grant program. They still used the term in 1980 and called it the basic grant program. Thirty-three percent had not.

Mr. **Simon**. Getting back to the calendar schedule, would that be of assistance to you at Northwestern University, shifting this calendar or just simply——

Mr. **Ihlanfeldt**. Several things would happen. First of all, we would eliminate a lot of the supplementary applications that are in the environment, and that would simplify the process, No. 1. No. 2, it would permit us to be able to not only say orally, but with some kind of chit or voucher, you do have money. We would attempt to again penetrate some environments that we frankly have found it extremely difficult to penetrate during the last 3 or 4 years. In the sixties and seventies one of my responsibilities changed—we went from less than 1 percent minority to 14 percent minority, quite a different distribution in terms of income on the campus. But since the change took place in the Pell program, and I recognize some of the data are soft and it is hard to draw positive facts, but when we reached the zenith in terms of financial aid we found that it was increasingly more difficult to penetrate some of the inner city areas. I think the Harvard study also comes to that conclusion.

Mr. **Simon**. Mr. Weiss?

Mr. **Weiss**. Thank you, Mr. Chairman. I am not sure if I understand the program or the point that you raised factually. I missed a witness who testified yesterday afternoon before the subcommittee for the Department of Education, but the report I had of their testimony was that their very complaint seems to be that applicants in fact are allowed to estimate what their adjusted gross income and their taxes paid have been. As a result they complained that there have been overpayments to Pell recipients by almost $300 million. Now, is there some discrepancy in my information, or are these facts as we understand it?

Mr. **Ihlanfeldt**. No. Let me give you my version. The rule as now applied to the financial aid process is no application can be submitted if you want to be eligible for Federal funds until after January 1. Many families complete that application and guess before they get their W-2 forms. They will complete it in January and still have not gotten to their IRS statement. If you follow the logic of the Department of Education——

Mr. WEISS. The form apparently provides for that kind of estimate to be made by the applicant, is that not correct?

Mr. IHLANFELDT. Well, it says in effect—I think there are four items, to extract this information from the 1040 forms, but not all families do that because they have not completed their 1040 forms.

Mr. WEISS. And they are allowed to estimate?

Mr. IHLANFELDT. They have no alternative but to estimate.

Mr. WEISS. No, it is not a matter of alternatives. My information is, according to DOE, the application form currently allows or authorizes the applicant to estimate what the taxes and income were for the preceding year. And they complain that because that is permitted they have been paying out too much money. You are saying that they are not allowed to do that, and as a result they have to wait until they have actually gotten their W-2's back, and by that time the whole sequence has run so late that they are disadvantaged, a very serious discrepancy it seems to me of a factual nature.

Mr. IHLANFELDT. If they complete their application after January 1, there is a reference that they should extract information from the IRS form. The fact is that many do not, and for that reason they operate on estimated income rather than actual income. Now the Department of Education, if you follow their logic, would like to move these applications back to April 15. I would like to move them forward with a verification document on the other side which would give you better validation. You would have 100 percent or universal validation in the example that I am suggesting.

Mr. WEISS. But you are starting with the premise that in fact the administration wants to follow through on the basic assumption of expanding opportunities?

Mr. IHLANFELDT. No, I am not assuming that premise whatsoever. I am simply stating that the initial intent of the program was to do that, and I think from 1973 to 1977 we were making good progress. In 1977 when we made a decision to delay the application process rather substantially I think it was attenuated or the progress began to slow up.

Mr. WEISS. But now if, in fact, DOE is asking for it, they get it either because of legislative changes or more likely because they are going to put in regulations which will change the form—never mind putting it into the position that you want, which is an estimate with verification.

Mr. IHLANFELDT. Or the use of prior year.

Mr. WEISS. Or prior year. Apparently what they want to do is eliminate altogether the capacity to work on any kind of estimate verification at all. They want absolute hard information as to what that income and tax criteria paid was and earned for the year—for that previous year, which is going to make the situation worse than it is right now, would you not say?

Mr. IHLANFELDT. If that is their intent, then I think it would destroy the original purpose of the program. If all the Pell program becomes is simply a subsidy to finance higher education, then it does not broaden one's horizons.

Mr. **Weiss**. I am advised by counsel that what they may be after is universal validation.

Mr. **Ihlanfeldt**. That is another matter, and that can be achieved in some of the ways that I have discussed. I understand they requested funds yesterday to do that. They want the financial aid officer on the campus to do it, and I would suggest there is a better way.

Mr. **Weiss**. Let me ask you a tangential point—I am sure that within your role you have come across it—what has been the impact, if you know, so far, on Pell grant applications of the elimination and phaseout of social security education benefits?

Mr. **Ihlanfeldt**. I do not know. I think it is too early to tell.

Mr. **Weiss**. What kind of——

Mr. **Ihlanfeldt**. We made estimates in terms of the cost on one single campus, but that is unrelated—that would vary from campus to campus.

Mr. **Weiss** [continuing]. Can you give us the information on the single campus?

Mr. **Ihlanfeldt**. $360,000 at Northwestern.

Mr. **Weiss**. At Northwestern?

Mr. **Ihlanfeldt**. Yes.

Mr. **Weiss**. Thank you.

Thank you very much, Mr. Chairman.

Mr. **Simon**. Thank you.

Mr. Erdahl.

Mr. **Erdahl**. Thank you, Mr. Chairman.

This also is a question that maybe goes beyond the scope of your testimony. I do not think it goes beyond the scope of your experience and expertise. This is a philosophical question, maybe a pragmatic one, as we are faced with budget cuts. Some say we have the option of emphasizing either the grants or the loans. Which way do you think we should pursue—guaranteed student loans, Pell grants, or some related thing?

Mr. **Ihlanfeldt**. Are you giving me an either/or question?

Mr. **Erdahl**. I am giving you an either/or question, but you can answer it any way you wish. I want to give you broad latitude.

Mr. **Ihlanfeldt**. I do not think that you can emphasize loans at the expense of grants, particularly if our intent is to broaden access in this country and to create greater opportunities. At the same time, there clearly have been abuses in the guaranteed student loan program that have to be resolved, and the one that I would recommend and have recommended since 1975 is that all guaranteed loans and the subsidy related should be on the basis of residual need only. Let us quit kidding ourselves; recent changes have created a lot of loans of convenience, and I do not think they are at all necessary. We became, frankly, in 1978 a bit too generous, and now we are going to live with those costs for a long time. But we should not throw the baby out with the bath water.

Mr. **Erdahl**. In other words, you are saying that maybe because of what was done several years ago, obviously those are costs that society and the taxpayers have incurred, the loans hopefully will be paid back over a period of time. But I take it you still endorse the concept that there are people that would not have an opportunity for higher education if they did not either receive the loans or the grants. One thing that has bothered me as we have looked at the cuts in education, that at some indefinable line, whether under pressure from the administration or coming out of Mr. Stockman's office or whatnot, in implementing the cuts we are making a fundamental social distinction that a family at a certain income level is not going to be able to send its son or daughter to school. Obviously there are exceptions. If you are below that level, you are not. Would you care to comment on that? Are there still resources available, so that the great American spirit will triumph and people will be able to find a way? I think you said maybe——

Mr. **Ihlanfeldt**. I would like to address that, but I want to make sure I say it correctly. First I think there needs to be a system in place that maximizes the current utility of funds available, and I do not think that is in place, and that is what I was addressing today. How do we maximize the use of those funds in an optimum way? Second, I think we have to look at those programs that have been extraordinarily costly, such as GSL, and ask ourselves where can we begin to change regulations, reduce benefits, without eliminating the program.

The principal ingredient of GSL, for example, is the guarantee, and some subsidy while a student is in school. The question of whether or not a student should receive or his borrower should receive a total subsidy while he is repaying is another matter altogether, so that is a choice that has to be made.

On the other hand, the Pell program has a specific purpose, and if the calendar is proper it will achieve that purpose. The supplemental grant program is very important if we are going to have access to private colleges and universities across this country for the people who have been disenfranchised in the past. Please keep in mind that many of these private institutions have invested millions of dollars of their own moneys over the last 15 years, and now they have the rug pulled out from under them. It simply means that they no longer can afford to participate in this society change and this transformation that has taken place, and we get back to what I would call the resegregation of American society.

Mr. **Erdahl**. Thank you very much for the specificity of your responses.

Thank you, Mr. Chairman.

Mr. **Simon**. Thank you. And we thank you very much for your testimony and for your suggestions.

Mr. **Ihlanfeldt**. Thank you, Mr. Chairman, for the opportunity.

Mr. **Simon**. Our final witness is Miriam Rosenberg, the legislative director for the Coalition of Independent College and University Students.

STATEMENT OF MIRIAM ROSENBERG, LEGISLATIVE DIRECTOR, COALITION OF INDEPENDENT COLLEGE AND UNIVERSITY STUDENTS

Ms. **Rosenberg**. Mr. Chairman, I am going to follow the text of my written testimony.

Mr. **Simon**. Proceed.

Ms. **Rosenberg.** Mr. Chairman, and members of the subcommittee, I appreciate the opportunity to appear before you to discuss some student concerns regarding the delivery system for student financial aid programs. My name is Mariam Rosenberg, and I am the legislative director of the National Coalition of Independent College and University Students (COPUS). The coalition, now in its seventh year, is a national student organization based in Washington, D.C., with State student associations and chapters at independent college campuses across the country.

Our primary concern, as students, is that the student financial assistance delivery system should allow for the limited amount of Federal funds allotted to student aid programs to be distributed in a manner that is as equitable, as timely, and as uncomplicated for students as possible. Several modifications of the current student aid delivery system are now being considered by the administration and the Department of Education. We believe that some of these modifications may unnecessarily disrupt the flow of Federal assistance to students who require those funds in order to attend college.

First, we are deeply concerned about the threat to prompt student notification of Pell grant awards posed by the potential for further reductions in fiscal year 1982 funding. Now that an acceptable family contribution schedule has finally been developed, we hope that any additional delays in the processing of Pell grant applications for the coming academic year will be avoided. Students must plan ahead for their school year budgets, and it is the intent of the forward-funding mechanism of the Pell grant program that they be enabled to do so. Rescissions and other budgetary developments should not impede the progress of this forward-looking awards process, this year or in future years.

Second, students, as the recipients of Pell grants or campus-based awards, strongly support the elimination of waste and fraud in those student aid programs, since that could help to insure the equitable distribution of program funds to those who most need it. We are concerned, however, that the proposed 100-percent validation procedure for Pell grant applications may create several problems for students.

Requiring financial aid officers to perform validation procedures on each eligible student's application will be an additional burden on the resources of an already busy office. This could only lessen the quality of financial aid services rendered to students by the office. The $5.2 million ($2 per verified application) that the Department believes will pay for administrative cost allowances to the institutions for validating the applications falls far short of easing the burden; a greater amount ($5 per application) was already authorized by the Higher Education Amendments of 1980, before any proposals for 100-percent validation procedures. Further, the Department has requested that $5 million of funds available for the Pell grant program in fiscal year 1982 be reprogramed to pay for the central processing costs of the proposed validation procedure.

We adamantly oppose using funds that were appropriated for the purpose of providing grants to our Nation's lowest income students, for the purpose of subsidizing a validation procedure that was not even in existence at the time of appropriation. If this validation procedure is deemed necessary by the Department, they may request a supplemental appropriation for that purpose in the next continuing resolution.

Finally, the proposed validation procedure raises many questions: Since many families do not file their tax return until April, will a validation procedure which uses the 1040 tax form create further delays in the processing of Pell grant applications? What will be the validation procedure for students (15 percent of the eligible students) whose families have incomes so low that they do not file 1040 tax forms? Is it legal to require families to divulge confidential income information on the 1040? Is it intrusion on the part of the Government to require the 1040 for validation purposes? Is the concept of 100-percent validation consistent with the administration's policy of reducing bureaucratic "red tape"? These and other questions are particularly difficult to answer, since the report upon which the entire validation proposal is based has not yet been released.

Third, the complexity of the application process for students filing several different financial aid application forms for several different programs is considerable. Moves toward simplification would be greatly appreciated by students, and could, perhaps, help to solve the problem of overawards in the various student aid programs which may be due, in part, to applicant confusion. Further, students should not be charged application fees for any of the programs. We oppose charging students money in order for them to prove that they are needy.

Our fourth concern is that endeavors by the Department to institute strict guidelines for satisfactory academic progress could result in a significant Federal intrusion into the academic requirements of individual postsecondary institutions, a practice which is shunned by the current administration. Colleges and universities around the country are now taking self-regulation initiatives which Dallas Martin and previous speakers spoke about which should prove to be an important move toward establishing adequate standards for satisfactory progress.

We are also concerned about the Department's proposals to change the definition of an independent student. Although students who are not fully independent should not be permitted to attain independent student status, stricter requirements must not exclude from eligibility those students who do not have any parental financial resources available to them.

Finally, COPUS perceives the overall lack of stability of the student aid programs as a major contributing factor to students' confusion surrounding these assistance programs—and confusion compounds the inaccuracies on applications which are later reported as "fraud and abuse" in the programs. We hope that the administration, the Department of Education, and Congress will take this factor into consideration as they deliberate further major alterations of all student aid programs.

I thank you again for the opportunity to discuss our views on these issues, and I hope that we may be of service to you in the future.

Mr. Simon. Thank you very much for an excellent statement. One of the things you touch upon that really meshes with the previous witnesses' testimony, and that is you speak about the complexity of the application process for students using various forms. Mr. Ihlanfeldt testified that I think it was 33 percent of all freshmen have not heard of the basic programs. I run into college and university groups who do not understand the financial aid programs, and it is no wonder that a student from a rural school in southern Illinois or an inner city school in Chicago gets totally confused by it all I think one of the things—and this goes beyond the immediate budgetary problems we are dealing with right now, but I think one of the things that this subcommittee has to deal with before too long is to see if we cannot simplify this procedure and make it clear to everyone in the Nation how you go about getting help for college.

Mr. Weiss.

Mr. **Weiss**. Thank you, Mr. Chairman. I have no questions. I do want to compliment the witness on her testimony. It was very clear.

Just a word on your last statement. Again you are assuming that in fact the administration wants more and more students to know how they can get help.

Mr. **Simon**. I am not making that assumption, Mr. Weiss.

Mr. Erdahl for the defense?

Mr. **Erdahl**. Mr. Chairman, I am not sure that I am the proper one to call for the defense.

I have a couple of questions. I would also concur that you have given us a fine statement today. Mr. Simon already touched on the complexity of the application form. Could we not have a simplification there?

I had another question that I should have asked the previous witness, but since you are here I will ask you. Where has the breakdown been in the failure of students to find out about these grants? Is that something that the colleges and universities themselves have failed to get their people onto the high school level? Has it been the high school guidance counselors, the teachers? Where is the breakdown? The previous witness said maybe half of the young people are not aware of the grants. Where has the breakdown occurred, in your opinion?

Ms. **Rosenberg**. I do not think I would have facts or figures but my feeling is it would have to be all of the above. If the high school guidance counselors do not understand the programs or are not aware of exactly how a particular student contemplating college would be aided by them, then the students are going to suffer. College financial officers certainly do not have the time to have a lot of outreach programs to students who are already in college to supplement the information that students may get on these programs. I think it is a combination of a number of factors.

Mr. **Erdahl**. Another you mentioned and you questioned is the validation procedure. Do you see ways that that probably could be done without discriminating and still be inexpensive to students and achieve some kind of accountability?

Ms. **Rosenberg**. I think I agree with some of the comments that have been made that the fact that people are using estimated data is a cause for discrepancies between any data on the application form and then later verification, validation. Perhaps the suggestion of the previous witness that we use previous-year data, which could be substantiated immediately with the application form and with an earlier application form so that the process could not have the delays that we have been experiencing, I think perhaps that is a solution. I am not an expert on that, so I would have to refer to others.

Mr. **Erdahl**. Sounds reasonable to me. Thank you very much.

Thank you, Mr. Chairman.

Mr. **Simon**. Thank you for your testimony. This concludes our hearing. We will resume our hearings Tuesday at 10 a.m.

[Whereupon, at 11:05 a.m., the subcommittee was recessed, to reconvene at 10 a.m., Tuesday, February 2, 1982.]

[Material submitted for inclusion in the record follows:]

COMPTROLLER GENERAL'S REPORT TO THE CHAIRMAN, SENATE COMMITTEE ON LABOR AND HUMAN RESOURCES

STUDENTS RECEIVING FEDERAL AID ARE NOT MAKING SATISFACTORY ACADEMIC PROGRESS: TOUGHER STANDARDS ARE NEEDED

Each year the U.S. Government provides billions of dollars in financial aid to students seeking a postsecondary education. While a wide array of assistance is available, the major programs are administered by the Department of Education (ED), the Veterans Administration (VA), and the Social Security Administration (SSA). These programs provided about $7.8 billion in student aid during fiscal year 1980. (See p. 1.)

There are no uniform requirements among the three Federal agencies regarding satisfactory academic progress of students receiving financial aid. VA requires an institution to establish and enforce a reasonable policy on satisfactory progress and meet specific requirements set by law and regulation. ED also requires that an institution set and enforce a policy, but does not provide specific criteria. SSA does not impose standards for academic progress in its program since there is no requirement set by law. (See pp. 2 to 8.)

In visits to 20 institutions of higher education and a review of more than 5,800 randomly selected student transcripts, GAO found that many students receiving financial aid were not making satisfactory progress. Mainly this resulted from school standards that allowed students to remain eligible for aid without proving that they were moving toward a definite goal with adequate grades and at a reasonable rate. Some of the institutions were not even enforcing their own standards. (See p. 9.)

GAO conducted its review in response to concerns raised in previous reviews of student aid programs on the adequacy of standards for determining satisfactory academic progress. After this review began, the Chairman of the Senate Committee on Labor and Human Resources expressed an interest in the issue and requested GAO to prepare a report on its findings for the Committee. (See p. 8.)

STANDARDS ARE NOT ADEQUATE

An effective academic progress standard should consider all factors which affect a student's academic performance. However, many of the schools visited did not have reasonable requirements concerning such factors as minimum grade point averages (GPAs), nonpunitive grades, and the rate of movement toward completion of a program of study. (See p. 9.)

While the schools visited uniformly required a 2.0 GPA (on a 4.0 scale) for graduation, they normally set their standards for determining academic progress at considerably lower levels. This resulted in large numbers of students on financial aid with low grades. Overall, 19.9 percent of the ED aid recipients, 23.1 percent of the SSA aid recipients, and 12.4 percent of the VA recipients in GAO's samples had cumulative GPAs below 2.0. In many cases, the averages were below 1.5, or the equivalent of a D-plus." (See pp. 9 to 12.)

The performance of many students in GAO's samples was distorted by their schools' overuse of nonpunitive grades—grades which have no effect on the GPA or do not count toward program completion. The schools often offered wide ranges of grades which had no effect on the measurement of progress. At two schools, nonpunitive grades accounted for more than 40 percent of all grades assigned during a recent term. (See pp. 12 and 13.)

A common example of a nonpunitive grade is that assigned for a course withdrawal. The schools visited often allowed students to withdraw from a course without penalty far into the term. GAO found many examples of students who had withdrawn from courses, allowing them to maintain higher GPAs, but also adding to the time necessary to complete a course of study. During the spring term of 1980, more than 20 percent of the ED and SSA aid recipients in GAO's sample withdrew from courses so that the number of hours they took was less than the number of hours required under their aid programs. (See pp. 13 and 14.)

Other nonpunitive grades were given for courses not completed or later repeated. Incomplete grades were often carried on a student's record for an extended time and, in some cases, were never converted. This resulted in higher GPAs than would have otherwise been the case. In some instances, students were allowed to repeat the same course numerous times. (See pp. 15 and 16.)

Only 10 of the 20 schools visited had specific requirements concerning the rate of a student's academic progress, and these requirements were often ineffective. This led to instances where students stayed in school and on financial aid for inordinate lengths of time. Among the ED aid recipients sampled, 56.3 percent of those attending school on a quarter system and 61.5 percent of those on a semester system were behind in their studies. (See pp. 18 to 20.)

In general, fewer instances of poor progress were noted among VA aid recipients than either ED or SSA aid recipients. GAO believes that this is due to the more stringent requirements set by VA, including (1) prior VA approval of a school's academic progress standard and a student's course of study and (2) refusal to pay for courses outside of an approved course of study, from which the student withdrew, or which did not count toward program completion. Neither ED nor SSA has such requirements. ED officials said they do not believe ED has the statutory authority to issue regulations setting specific requirements. There are no statutory requirements for academic progress in the SSA program. (See pp. 3 to 8.)

STANDARDS ARE NOT ENFORCED

Nonenforcement of academic progress standards is a major problem. Nine of the schools visited were not enforcing their published standards. Three schools were not enforcing their standards for ED or VA aid recipients, five schools were not for ED aid recipients only, and one school was not for VA aid students only. SSA had no academic progress requirements. (See pp. 22 and 24.)

For the schools which had not enforced their standards for ED aid recipients, GAO estimated overpayments of about $1.28 million. GAO did not project overpayments for VA recipients because the schools did not have information on the amount of financial aid paid by VA. (See pp. 22 and 23.)

CONCLUSIONS

Weak and nonspecific Federal requirements on academic progress have led to abuse of the student aid programs, particularly those administered by ED and SSA. A uniform Federal policy is needed. Although VA standards set by existing legislation and regulations are generally adequate, standards are needed for the rate at which a student is progressing. GAO believes that ED and SSA requirements should be essentially the same as those set by VA. This would require changes to both authorizing legislation and program regulations. (See pp. 25 and 26.)

These changes would accomplish the following objectives:

Tighter academic progress standards would save Federal funds now being paid to students not making satisfactory progress.

Schools would encounter fewer differences in the requirements for administering the three agencies' programs.

Federal agencies would be able to better coordinate their efforts in setting academic progress requirements and monitoring their enforcement.

Also, students might be encouraged to enroll in programs which are more suited to their abilities and which they are more likely to complete. (See p. 26.)

RECOMMENDATIONS TO THE CONGRESS

In a previous report (see p. 7), GAO recommended that SSA student benefits for postsecondary students be discontinued. The Congress has provided for the discontinuance of these benefits in the Omnibus Budget Reconciliation Act of 1981. Since the program will be phased out over a 4-year period, however, GAO believes there is a need for academic progress requirements for students who continue to receive SSA benefits. Therefore, GAO recommends that the Congress amend the Social Security Act to require students receiving postsecondary education benefits to maintain satisfactory progress in the course of study pursued, according to the standards and practices of the school attended. GAO also recommends that the Congress amend the Social Security Act and the Higher Education Act of 1965 to authorize SSA and Ed to issue regulations setting forth general requirements for institutions of higher education to follow in establishing academic progress standards. (See p. 27.)

RECOMMENDATIONS TO THE SECRETARY OF EDUCATION AND THE SECRETARY OF HEALTH AND HUMAN SERVICES

If the Congress amends the legislation as GAO recommends, the Secretaries should issue regulations setting forth general requirements that institutions must meet in establishing academic progress standards for postsecondary students receiving ED and SSA financial aid.

These regulations should specify that an institution establish, publish, and enforce academic progress standards for students receiving aid, subject to the agencies' review and approval. While the regulations should allow each institution discretion in setting its own standard, the school's standard should provide for

a reasonable relationship between the minimum proficiency levels or GPAs required and the requirements for graduation or program completion;

movement toward graduation or program completion at a reasonable rate;

limitations on excessive withdrawals, repeated courses, courses for which nonpunitive grades are assigned, and courses that do not count toward graduation or completion of a program; and

application of the standard on a timely basis, preferably at the end of a grading period.

The school should also be required to show (1) how the academic progress standard relates to the school's probation/suspension policies and (2) what a student has to do to have aid reinstated. (See p. 28.)

RECOMMENDATION TO THE ADMINISTRATOR OF VA

The Administrator should issue regulations, supplementing those now in effect, to require institutions of higher education to include provisions in their academic progress standards which would require students to move toward graduation or program completion at a reasonable rate. (See p. 28.)

RECOMMENDATION TO THE DIRECTOR OF THE OFFICE OF MANAGEMENT AND BUDGET

The Director should ensure that ED, SSA, and VA coordinate their efforts in setting and enforcing requirements for academic progress standards under student financial aid programs in an effort to improve administration at both the Federal and institution levels. (See pp. 28 and 29.)

AGENCY COMMENTS AND GAO'S EVALUATION

HHS and OMB generally agreed with GAO's recommendations. HHS questioned, however, the usefulness of implementing standards for its program, which is being phased out. VA did not agree with GAO's recommendation, claiming it would be unworkable and an administrative burden. (See apps. VI, VII, and VIII.) GAO did not agree with either agency. (See p. 29.) ED was given the opportunity to provide comments on a draft of this report. It had not done so when the 30-day statutory comment period expired and this report was finalized.

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OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

TUESDAY, FEBRUARY 2, 1982

House of Representatives,
Subcommittee on Postsecondary Education,
Committee on Education and Labor,
Washington, D.C.

The subcommittee met, pursuant to call, at 10:20 a.m., in room 2257, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Peyser, Erdahl, and DeNardis.

Staff present: William Blakey, staff director; Maryln McAdam, legislative assistant; Betsy Brand, minority legislative assistant, and John Dean, minority counsel.

Mr. Peyser. This hearing will come to order.

Chairman Simon has been delayed for a brief period of time but he will be with us shortly. In the meantime, Mr. DeNardis and myself will get the hearing underway.

This begins the second week of oversight hearings on major Federal student assistance programs.

This morning we will hear from the executives of three State guarantee agency heads who will contribute to our knowledge of the Guaranteed Student Loan and Auxiliary Loan programs.

We will hear some suggestions on how we can improve these programs within current cost constraints.

I would like to enter Chairman Simon's statement for the record.

[Opening statement of Hon. Paul Simon, chairman.]

Opening Statement of Hon. Paul Simon, a Representative in Congress From the State of Illinois and Chairman, Subcommittee on Postsecondary Education

Good morning. The Subcommittee on Postsecondary Education begins its second week of oversight hearings on the major Federal student assistance programs. This morning we will hear from the executives of three state guarantee agency heads who will contribute to our knowledge of the Guaranteed Student Loan (GSL) and Auxiliary Loan programs. We will hear some suggestions on how we can improve these programs within current cost constraints.

I want to emphasize the last point because I think it is clear that we are not in an era of expansion. With the Administration contemplating further massive reductions including:

Eliminating graduate and professional school student eligibility in the Guaranteed Student Loan program;

Eliminating the Supplemental Educational Opportunity Grant and the National Direct Student Loan (capital contribution), while reducing the College Work Study program by more than $100, and finally;

Reducing funding for Pell Grants by $1 billion below the fiscal year 1981 appropriation.

I intend to oppose these changes and the recommended reductions. I believe most of my colleagues share my views and will work cooperatively to find responsible savings and seek sound legislative solutions which will maintain a viable set of Federal student assistance programs. These programs are important to sustaining the Nation's commitment to educational opportunities for low and middle income students. They are also critical to maintaining diversity among public and private postsecondary institutions.

I know that several of our witnesses today have specific suggestions, while others have information which will guide our thinking. I look forward to hearing from each of you.

Mr. PEYSER. I think that one of the most critical things for all of us who are involved in this week and who are concerned about what is happening falls right on that line of the constraints that are being placed on the education community by this administration. It is something that we have to, (1), learn to, if we can't win the battles, to work effectively within them.

And then, (2), by the knowledge we learn of what is happening out there from the people who are going to be testifying, of seeing, perhaps, if we can restrict further cuts in these programs. That is going to become of tremendous importance to all of us.

Now, having said that, I will defer to Mr. DeNardis if he has any opening remarks and then we will get our hearing underway.

Mr. DENARDIS. Mr. Chairman, no, I don't. Let's commence.

Mr. PEYSER. Very good. The first panel includes Mr. Joseph Cronin, president of the Massachusetts Higher Education Assistance Corp. from Boston, Mass.; Richard Hawk, president of the Higher Education Assistance Foundation, Overland Park, Kans.; and Dr. Dolores E. Cross, president of the New York State Higher Education Service Corp.

I would suggest for the benefit of all who will be testifying, your entire statements will be put into the record. You may either read them, summarize them or handle this in any way that you see fit.

I would also like to remark on the importance of these types of hearings and these programs to the public was well illustrated to Mr. Cronin and myself just 2 weeks ago in Massachusetts when I was speaking at a program in Framingham at Framingham State College. There was a blizzard going outside, and with all sorts of travelers' warnings of people to stay home, we had a couple hundred people who were in that place. They came out regardless, because of their concern.

It was a very graphic demonstration to me of how the public feels and is concerned on these issues.

So, Mr. Cronin, if you will lead off, we would be delighted to hear from you.

Incidentally, we will hold any of our questions until the panel has completely testified and then we will have questions.

STATEMENT OF JOSEPH M. CRONIN, PRESIDENT, MASSACHUSETTS HIGHER EDUCATION ASSISTANCE CORP., BOSTON, MASS.

Mr. CRONIN. Thank you, Congressman.

I was asked if I would comment in particular on the experience with the PLUS program, that being one of the newer programs and one that we implemented at the first possible opportunity in Massachusetts on January 2 a year ago. We have had, perhaps, a little bit of a headstart and have a few suggestions to make about both the Parent Loan program and on the amendments which have been called the Auxiliary Loans to Aid Students, ALAS.

I believe my colleagues will probably speak on other aspects of the guaranteed student loan program although they may have some comments on PLUS as well.

We are going to differentiate, at least in my testimony, between the PLUS program and the ALAS.

The parent loan program for undergraduate students, we think achieves the objectives established for it by Congress in 1980 and only a few changes are needed to perfect PLUS.

But the ALAS program is a disaster. Very few banks wish to participate in such a poorly designed, low yield, uncertain program, and any thoughts of putting all graduate professional school students on ALAS should be summarily dismissed as unworkable, unwise, and unfair to students and schools.

The ALAS program, if it is to survive at all, needs major repairs beginning with the unfortunate acronym and including practically every major structural component.

Now, why does PLUS pass and ALAS fail? Well, first of all, the PLUS program was created not as a substitute for the GSL but as a supplementary program, mainly at the request of the higher cost, independent colleges of which we have very many in the Northeast.

For example, of the first 6,000 parent loans that we have guaranteed in Massachuetts, 94 percent of them went to aid parents to pay for tuitions at 4-year colleges and 84 percent of them were for tuition at independent colleges and universities.

How does the program work? I will just give you some of the highlights. We do ask for a credit check. We ask the banks to perform this just as they would for any other personal or consumer loan using due diligence. And more than 95 percent of the applicants have proven to have satisfactory credit histories and to begin repayment within 60 days at at least $50 a month.

That is the essential ingredient of the PLUS program and that is why it costs less to the Federal Government.

We have had on 6,000 loans only three insurance claims to date, all of them related to the death or disability of the borrower. There have been no financial defaults.

I understand you have at least one bank testifying. They will tell you that the PLUS program requires somewhat more work than the guaranteed student loan because the loan goes into repayment right away and because of the credit check.

However, our banks say that they have been very much impressed by the quality of borrower and by the fact that this generates additional business for the banks.

So, we have about one-third of our lenders in Massachusetts, 125 who have joined the parent loan program in the first year. It took us 25 years to get 380 lenders in the student loan program.

We think we are making good progress in recruiting banks.

We had a national conference in Denver a few weeks ago with the 23 States that have already joined the parent loan program. Many of the 25 States that are planning to join it this spring and summer attended and we exchanged information.

We are not too happy about the raising of the rate last October from 9 percent to 14 percent. We thought this might choke off new borrowing, but it did not. Since October we have had 1,000 parent loans processed. We have had excellent cooperation from the colleges and universities in terms of processing these loans.

We have made them to 450 schools all over the Nation, in Massachusetts and outside. I mention some of the colleges in my testimony.

Now, what changes should be made in PLUS? What specific proposals should this committee of the Congress consider? One flaw that we see is the proposal to hold the interest rate firm for 1 year even after the Treasury bill falls below 14 percent as it did last October.

If that provision stays in, it means that next summer when the President's economic program is working and inflation curtails and interest rates are down to 8 or 9 percent we are going to have this sky-high 14-percent program.

So what the committee needs to consider is some kind of trigger mechanism or twice a year readjustment mechanism which I think you can build in, probably taking about a paragraph, to adjust the interest rate perhaps twice a year. People think in terms of Treasury bills and first quarter, second quarter.

The ideal times would be the end of the second quarter which would be the beginning of the summer season and then at the end of the year. We do have some second semester or January loans. We do have a number of students, students who begin their academic work in January of each year.

So those are two good points to adjust it and we should not wait the 12 months.

That provision which was hastily put together during the August conference committees was copied almost verbatim from the GSL language on 9 percent going down to 8 percent.

Well, that was so far below market that that is not a serious problem but it is for a loan so close to market rates as is the PLUS loan.

Just as an example, in June and December, if the T-bill were below 14 percent, this should trigger a 12-percent PLUS loan rate. If below 12 percent, it should trigger a 10-percent PLUS and eventually go to 8 percent and maybe below if the Claremont economics people are correct with some of their predictions but I did not want to overload the circuits at this particular hearing.

The second change is to take a look at the loan limit. Three thousand dollars a year was OK as we moved into the 1980's but with universities and colleges playing catch-up ball with tuition and faulty salaries it would be better to make a word change and say $3,000 a semester rather than $3,000 a year with a maximum eligiblity of $6,000. Mind you, this will still be less than half of the total cost of education at many of our fine colleges in the Northeast which are going to go up next year to $12,000 and $13,000.

Many of these families may not be eligible for the guaranteed student loans. So, this is a serious proposal, especially important if some of the other grant programs are further curtailed this year.

A final recommendation on approving the PLUS program, the law should authorize the use of credit life insurance by State guarantee agencies to reduce claims due to death.

Now, this is not as serious an issue for the GSL. We find that our parents participating in the program range in age from the late thirties right up into the seventies.

Actuarily the chances of some of our older PLUS loan recipients making it through the 10th year are just a little bit shaky. But life insurance would be a very modest addition of cost maybe 40 or 50 per $1,000 and would protect both the Federal and State guarantee agencies.

It sounds like a modest change but it would help curtail the cost to the Federal Government.

The auxiliary loan program, ALAS, we have found no lenders ready to make these immediate repayment loans to students who may have no money to repay and who have the right, under the law, to ask for deferments from payments right away. It is just contradictory. The illogic is built in.

The acronym, ALAS, itself, deplorable and perjorative, even the Department of Education refuses to use it and we agree with that.

In fact, we suggest that this label be dropped immediately, this being the only change that could take effect at once without causing severe problems.

Now, we have tried to make ALAS work in Massachusetts. We had a work conference with 15 lenders and 30 graduate professional school aid administrators to see how it could go. After 3½ hours of tense discussion we said, look, what really makes sense, and this is ideal, is a provision allowing a graduate student to demonstrate need for and obtain up to $8,000 a year for graduate professional studies under the graduate student loan program. This is the right solution.

We realize it is more costly to the Federal Government than the existing $5,000 limit but it is needed by students in our part of the world attending graduate professional programs costing as much as $11,000 to $18,000 a year.

The Tufts New England Veterinary Medicine School costs $18,500 a year tuition this year and of that some of the States buy seats for about $8,000 or $10,000 leaving those students with a borrowing need of up to $8,000 a year. That is the only veterinary medical school in New England.

Second, the next preference would be to redesign the programs the parent loans to undergraduate and graduate students. Several of our bankers have proposed this. The acronym would be called PLUGS, which, of course, fills the gap. With the graduate component exactly parallel to the PLUS program except for the right to ask for deferments could be eliminated and up to $6,000 a year per student could be loaned with a payment to begin within 60 days.

Now, this works for the younger graduate students, not for the older ones who may be married, in which case a paragraph could be added saying that a working spouse, there has to be somebody creditworthy and able to repay would substitute for the parent if one was not willing or available to take out the loan.

The third possibility would be to allow discounting the loans such as is common in many consumer loans. That is to say for a 1-year master's you could pay the interest up front from the loan proceeds.

This would require an exemption from the truth-in-lending disclosure which is an idea whose time may have come for the GSL as well, this program being rather tightly regulated by the Congress as it is and with a number of unconventional features such as deferments and origination fees and the like.

Every time we have to change the promissory note and that was three times in the year 1981, the program changed in January and August and October, we have to go and redesign the computer which produces the promissory notes and then get all the signoffs from State and Federal officials in terms of disclosures and truth in lending. It is very cumbersome.

Another progressive proposal is to merge the PLUS and HEAL program. Last year the HEAL program rose at an interest rate of above 19 percent. We should not call this the HEAL program but the gash or wound or maim program, anything but HEAL because it is absolutely unhealthy. I got that idea from some of your folks in New York State.

The 14-percent interest rate should be the highest that anyone would pay for any of our graduate programs. There is a possibility for consolidation or merger.

Again, the most serious criticism we would have of making graduate students pay for their loans while they are in school is that by the second year in a doctoral program or law school program or any master's programs, the interest alone on two ALAS loans would be $840 a year, $70 each month. By the third year, $105 a month or $1,260 a year.

Our colleague, Col. Robert Ziegler, head of the Ohio agency, within moments of hearing this scheme, said this would provide the "quick, slick road to default."

We feel strongly that if a nation is to invest in the scientific, engineering, medical, management and educational expertise that we require, that this is not the time to relinquish quality in these fields and discourage enrollment.

In the help wanted ads that the President of the United States referred to at a recent press conference, 22 out of 24 pages were for highly qualified and educated professionals, the kind who graduate from these specialized schools.

We must not now forsake the most ambitious and most intelligent students in America.

Thank you.

Mr. **Peyser**. Thank you very much for your testimony.

[The prepared statement of Dr. Joseph M. Cronin follows:]

PREPARED STATEMENT OF DR. JOSEPH M. CRONIN, PRESIDENT, MASSACHUSETTS HIGHER EDUCATION ASSISTANCE CORP., BOSTON, MASS.

PARENT AND AUXILIARY LOANS

The PLUS program, Parent Loans for Undergraduate Students, achieves the objective established for it by Congress in 1980. Only a few changes are needed to perfect PLUS.

The ALAS, Auxiliary Loans to Aid Students, is a disaster born of last summer's reconciliation process. Very few banks wish to participate in such a low-yield, poorly designed program. Any thoughts of putting all graduate and professional school students on ALAS should be summarily dismissed as unworkable, unwise and unfair to students and schools. ALAS needs major repairs beginning with the unfortunate acronym and including practically every major structural component.

Why does PLUS pass and ALAS fail?

PLUS was created as a supplementary program, mainly for higher cost independent colleges. Of the first 6,000 PLUS loans in Massachusetts 94 percent went to pay for four-year colleges and 84 percent paid for tuition at high-cost colleges.

Parents were asked to submit routine credit information for analysis identical to that which would be required for a personal or consumer loan to employed adults. More than 95 percent of applicants proved to have satisfactory credit histories and the capacity to begin repayments of at least $50 a month within sixty days of disbursement of the loan. MHEAC has paid only three insurance claims on over 6,000 PLUS loans, all relating to the death or disability of the borrower. There have been no financial defaults.

Banks report that PLUS loans require more work than guaranteed student loans because of the credit check and the immediate collection activity. However, this is offset by the excellent quality of borrowers and the variable rate tied to the Treasury Bill which carried a total yield of 19 percent for two quarters in 1981 and 16 percent for the fourth quarter.

Our largest PLUS lender reports an increase in other banking business from PLUS borrowers.

One hundred and twenty-five lenders have joined the PLUS program compared to 384 lenders in the G.S.L. program.

The 9 percent rate was quite popular, but the change to 14 percent was accepted. We have guaranteed more than 1000 PLUS loans since October 1st, 1981 when the rate changed. Some 450 schools processed PLUS loans. Fourteen of the top twenty universities were in Massachusetts and included Boston College, Boston University, Northeastern, Harvard and the University of Massachusetts. Others included Brown, Syracuse, Providence College, Colby College and the Universities of Vermont and New Hampshire.

Colleges in the Northeast, both high tuition independent colleges and the major land-grant universities, have cooperated to expedite the processing of these loans. College administrators welcome the cash flow and the assistance to families with two or three students in college at once.

What changes should be made in PLUS?

1. Consideration should be given to a proposal to adjust the interest rate at least twice a year at the end of the second quarter and the end of the fourth quarter (two critical points for volume). As inflation subsides and the Treasury Bill falls below 14 percent, it should not be necessary, as under the 1981 Amendments, to wait twelve months for the downward adjustment. This timetable, copied almost verbatim from language used in the G.S.L. 9 percent to 8 percent transition, is too rigid for loan rates set so close to market level. The June and December 91-day T-Bill, if below 14 percent, should trigger a 12 percent PLUS rate, and if below 12 percent, should trigger a 10 percent PLUS rate, and eventually go to 8 percent.

2. The loan limits for PLUS should provide for $3,000 a semester or $6,000 a year for the academic year 1982–83. More than one hundred colleges now cost $10,000 a year or more to attend. Several colleges will this year announce $13,000 in total tuition, fees, room and board, and transportation. A student loan of $2,500 and a parent loan of $3,000 may have been adequate for 1978 college costs, but not for 1983 prices. If Pell grants are further reduced, loan eligibility for middle income families limited, and work opportunities remain constrained, the pressure on families to borrow more will be enormous.

3. The law should authorize the use of credit life insurance by state guarantee agencies to reduce death claims on PLUS loans. It would be discriminatory to deny loans to parents in their sixties or seventies (our agency has guaranteed three PLUS

loans to septuagenarians). It may cost as little as $.40 per $1,000 to obtain credit life coverage to cope with actuarial inevitabilities.

The ALAS or Auxiliary Loan program in Massachusetts, alas, in 1981 found no lenders willing to make "immediate repayment" loans to students who may have no money to repay and who have the right to ask for deferred repayments. Any program so illogical and contradictory is unlikely to succeed. The acronym ALAS itself is deplorable and pejorative. Even the U.S. Department of Education refuses to use it. My agency suggests it be dropped immediately this being the only changes which could take effect at once without causing severe problems.

On January 15 thirty Massachusetts financial aid administrators for graduate and professional schools met with fifteen lenders to see how the ALAS program might be made to work. There was a general consensus that:

1. What makes more sense is a provision allowing a graduate student to demonstrate need for an obtain up to $8,000 a year for graduate and professional studies under the Guaranteed Student Loan Program. This is more costly to the federal government than the existing $5,000 limit, but it is needed by students attending programs costing as much as $11,000 to $18,000 a year.

2. The next preference is to make Parent Loans to Undergraduate and Graduate Students (PLUGS—to fill up a gap) with the graduate component exactly paralleled to the PLUS program except that deferments could be eliminated. Up to $6,000 a year per student could be loaned with repayment to begin within sixty days. A working spouse or guardian could substitute for the parent if one was not willing or available to take out the loan.

3. Another improvement would be to allow discounting of the loan such as is common to many consumer loans (one year interest paid up front from the loan proceeds). This requires an exemption from the Truth-in-Lending disclosure which is an idea whose time has come for the GSL as well. The purposes of Truth-in-Lending are satisfied by the tight regulation of both programs and the unconventional nature of these loans (i.e. deferments, origination fees, differing interest rates, etc.)

4. Congress should consider merging the PLUS and HEAL programs. Charging future doctors and dentists as much as 19 percent last year unhealthy and is scaring lenders almost as much as it wounds the student. The 14 percent interest rate should be the universal maximum with parents (or spouses) encouraged to make interest payments during the in-school period.

Most of all, it must be realized that many graduate students have very little money and cannot pay even the interest on two loans ($840 a year, $70 each month) while in school the second year, or $1,260 or $105 per month in the third year. Such a scheme is, as Colonal Robert Ziegler of the Ohio agency vividly suggests, "the quick, slick road to default."

The nation must invest in the scientific, engineering, medical, management, and educational expertise which we require. This is not the time to relinquish quality in these necessary fields. The help wanted ads emphasize the need for highly qualified and educated professionals. We must not now forsake the most ambitious and most intelligent students in America.

Mr. **Peyser**. Next we have Richard Hawk.

STATEMENT OF RICHARD C. HAWK, PRESIDENT, HIGHER EDUCATION ASSISTANCE FOUNDATION, OVERLAND PARK, KANS.

Mr. **Hawk**. Thank you very much, Mr. Peyser.

This is a very serious matter. There is a great deal which needs to be said. Accordingly, Mr. Chairman, my written testimony is longer than I would like for it to be. I shall not burden the reading of that but I shall make comments on that written testimony.

Mr. **Peyser**. Thank you.

As I stated it will all be entered in the record.

Mr. **Hawk**. Thank you.

There is contained in that testimony a plan for reducing Federal expenditures for the guaranteed student loan and I do refer to reducing Federal expenditures rather than reducing costs because the fact of the matter is that there is relatively little, if any, opportunity to reduce costs of the program.

Hence, when one talks about reducing costs, one is really talking about reducing Federal expenditures. Reduction of Federal expenditures can come through one of two alternatives, both of which are, frankly, undesirable.

One is to restrict the volume of loans on which the Federal Government incurs costs, thereby reducing opportunity for the citizens of this Nation to have access to postsecondary education.

The other alternative is to simply transfer the cost from the Federal Government to other parties, in particular the borrowers and students who need assistance to begin with.

Nonetheless, I am advancing a plan which would provide for reduction in Federal expenditures in amounts approximating $750 million over the life of loans originated next year.

Assuming that volume would remain relatively constant, another $750 million would be saved over the life of loans originated in the subsequent year following and thereafter.

The plan has two components, Mr. Chairman. The first, of which involves elimination of the new origination fee with a substitute in its place of a change in the reinsurance arrangement.

I am sure we are all gratified to see Mr. Simon arrive.

Mr. SIMON. My apologies. I have just come from the airport and there is nothing I can do about those things.

Please continue your testimony and my apologies for getting here late.

Mr. HAWK. Mr. Chairman, I just said to the committee that the plan which is contained in my written testimony would provide savings on the order of $750 million over the life of loans originated next year and another $750 million over the life of loans originated in each year thereafter.

The plan has two components, the first of which involves elimination of the origination fee and a replacement of that origination fee with a change in the reinsurance arrangement.

The proposed change in the reinsurance arrangement would generate net savings after elimination of the origination fee of in excess of $140 million over the life of the loans to be originated next year.

Moreover, the change in the origination fee which would involve an increase in guarantee fees, fees which are charged by guarantors to student borrowers would not result in a net increase in costs to student borrowers because with the elimination of the origination fee the student, on average, comes out the same.

So that component of the plan results in significant savings over the life of loans originated in each year and does not cause an additional cost burden on the average to the student.

The modification of the reinsurance arrangement, essentially says that we should discontinue the practice under which the Federal Government always carries the initial and major burden with respect to defaults and we should place that burden on the guarantee agency.

As you know, at the present time the Federal Government reimburses guarantors for 100 percent of all claims for death, disability and bankruptcy and 100 percent of the first 5-percent of defaults which occur in each year with the determination of that 5 percent default rate being based on a comparison of loans which go into default in that year with loans which happen to be in repayment in that year.

Next year the cycle starts over again with the first five percent being fully reimbursed by the Federal Government.

This proposal is to turn that around and cause the first defaults in each year or the first defaults with respect to any loan portfolio to be borne by the guarantor with reimbursement by the Federal Government coming in only as default rates increase.

Now, to achieve this kind of arrangement we would need to change the basis on which we calculate default rates. We could do that by saying that all loans originated in 1 year constitute a portfolio.

What we will look at is the percent of those loans which go into default over the life of that portfolio.

So, if we have $10 of loans originated in one year, one dollar of those loans goes into default sometime. The default rate on that portfolio is 10 percent. With this mechanism the plan proposes that there would be no Federal reimbursement of claims, including claims for death, disability and bankruptcy for the first 5 percent of defaults or nonpayment on that portfolio, with a sliding scale which would provide for 100-percent reimbursement only at the bulk rates or claims rates including death, disability, and bankruptcy, get above 12 percent.

It is just the reverse of what is happening now. What is happening now is the Federal Government always picks up the burden of the defaults on the front end and that is a costly proposition for the Federal Government.

An additional advantage to that kind of arrangement would be that the Federal Government would be placing greater responsibility and hence accountability on guarantee agencies, No. 1.

And, No. 2, the Federal Government would be providing a genuine, realistic financial incentive for guarantors to address the default rate.

I am not suggesting that guarantee agencies do not address default rates effectively now, but I am suggesting that the incentives are backward.

The guarantee agency has a real financial incentive to reduce defaults now only after defaults have already gotten hot because you start out with the Federal Government always providing 100-percent reimbursement.

I am proposing to turn that around.

The guarantor agency would have to bear the burden and utilize its own funds for that initial default and hence it would have a financial incentive to be concerned about the default rates from the beginning.

That is the first incentive of the plan as it is presented. I think it has important advantages in terms of incentives to keep default low, placing an additional responsibility on guarantor agencies. With the elimination of the origination fee it would achieve savings without increasing the cost to the student.

The second component of that plan, Mr. Chairman, if I may, involves the area of the guaranteed student loan which is the most expensive for the Federal Government and that is the special allowance payment which is paid to lenders.

As you know, at the present time, the special allowance payments vary with the 91-day T-bill rate without limitation. This, of course, causes financial strain for the Federal Government during periods of high interest rates.

It is possible to shift the burden or the risk of fluctuations in interest rates from the Federal Government to the borrower, hence, putting the student borrower in much the same situation as other borrowers in the economy.

The cost of money to them would vary with general market interest rates.

Now, this can be done without having a variable interest rate paid by the student. The way in which it could be done would be by increasing the rate at which interest is charged to the student to 14 percent but permitting the cost of interest as opposed to the rate to vary as general interest rates in the economy go up and down, through a mechanism under which a portion of a standard 4-percent special allowance, a portion of that would be allocated to loan principal depending upon what the level of interest rates were.

The effect of this would be that the student would be making repayments based on a 14 percent interest rate. The Federal Government would be providing a standard 4-percent special allowance. That would not fluctuate. There would be a calculation every quarter just as there is now based on the 91-day T-bill rate.

The purpose of that calculation no longer would be to determine the amount of the special allowance which the Federal Government pays but rather to determine what portion of that standard 4-percent special allowance which is being paid to the lender should be allocated to repayment or reduction of loan principal as opposed to being used as an interest supplement.

The effect of that is as interest rates decline, larger portions of that standard 4-percent special allowance payment gets allocated to reduction of loan principal, thereby reducing the effective rate or the effective cost of that loan to the student.

I know, Mr. Chairman, and members of the committee, that in a first passing that sounds like a somewhat complicated formula.

In actual fact it is probably no more complicated than the concept which we now have gotten very used to and seems very simple that we have a special allowance which is the 91-day T-bill bond equivalent rate minus 3.5, or minus 5.5, or minus 7.5, whatever, depending upon the interest rate which determines what the return to the lenders would be.

The concept which I am talking about is really no more complex than that. It seems more complex than that at the outset because it is a new concept and one with which we have not worked.

Now, the savings from that kind of an arrangement would be in the neighborhood of $600 million over the life of all of the loans originated next year. Another $600 million would be saved over the life of loans originated in the following year and it is the combination of that $600 plus million dollars with $140 million in the other component of the plan which would yield the savings in the amount of $750 million over the life of loans originated in 1 year.

Now, Mr. Chairman, I think we should keep in mind the words of Thomas Jefferson when he said that nothing more than education advances the power, the prosperity and the happiness of a nation, nothing more than education.

I think we should also keep in mind that it was the leaders of past generations in keeping with this kind of philosophy which provided the basis for the economic development, the richness of life and the sophisticated civilization which this generation enjoys now because of their continuing emphasis on increasing educational opportunities as a basis for developing this kind of a sophisticated and profitable society.

I think we should also keep in mind that it was the sacrifices of past generations which provided this Nation with an impressive array of colleges, universities, and full secondary educational technical institutions which do, indeed, provide marvelous opportunities for the citizens of this Nation.

But the reality is that opportunities without economic access are not opportunities at all. And when we begin to restrict volume of a program like the guaranteed student loan we are eliminating economic access which means we are, in fact, denying those kinds of opportunities.

Now, the guaranteed student loan is not a giveaway program. It is a program which permits individuals to assume responsibility for the cost of their own education. Society, through the Federal Government, recognizing the benefits of having an educated citizenry, provides the mechanism to permit those individuals who are going to benefit directly to pay for their own expenses through payment from earnings after the educational experience rather than from resources at the time.

So, I would urge you, Mr. Chairman and members of the committee, to keep these kinds of principles in mind as you consider cost-saving measures.

Now, my testimony does propose some criteria against which you could evaluate different kinds of cost-saving plans and they are in priority order.

It says that, No. 1, you ought to be concerned about whether or not any plan reduces access to full secondary education and if it does, rank low.

No. 2, you ought to be concerned about the impact that a plan would have on the ability of the participants in the delivery of a product to perform effectively. If it diminishes that, it probably ought to rank low.

Third, keep the program as simply as possible but not just for the sake of simplicity because it is obviously more important to meet needs.

Fourth, you ought to be concerned about the cost to the student. The reason the cost to the student is ranked last is because of the conviction that it is better to provide an opportunity at a higher price than it is to eliminate the opportunity.

So, if the committee and the Congress had to make a choice, if you had to make a choice should we restrict loan volume and deny opportunity or should we create a modification which increases the price to the student but still preserves that opportunity, it seems to me that every time you ought to opt in the direction of preserving that opportunity.

Mr. Chairman, my written testimony also includes some reactions to other possible plans for cost savings. We periodically hear things like, well, we ought to eliminate the tax exemption on student loan revenue bonds. That, Mr. Chairman, would be a disaster in at least 20 States in this Nation.

Those States which are not major money market centers cannot provide the total amount of capital which is needed to meet this kind of a need.

There are reactions in my testimony to the other possible approaches and there are some suggestions with respect to the PLUS program as well.

Mr. Chairman, I would like to make it clear that in advancing this plan for reducing Federal expenditures for the guaranteed student loan program, I am doing so only because it seems to me it is essential that this kind of program be continued and if, indeed, the priorities of military spending and tax reduction require it, if the pressures from those are so great that the program has to be reduced, I want to make any contribution that I can to assist you in making responsible decisions which will preserve opportunities to the maximum extent possible.

Thank you.

Mr. SIMON. Thank you very much for your testimony.

[The prepared statement of Richard Hawk follows:]

PREPARED STATEMENT OF RICHARD C. HAWK, PRESIDENT, HIGHER EDUCATION ASSISTANCE FOUNDATION

This testimony is intended to provide constructive suggestions on reducing costs to the federal government of the Guaranteed Student Loan Program. The offering of these suggestions is not intended to imply that federal expenditures for guaranteed student loans are higher than can be justified in terms of benefits of the program, that federal expenditures for this program are not being put to good use, or that the return on the investment in the form of future contributions by those who are assisted by the program is less than adequate.

On the contrary, current and projected expenditures for the program as presently structured represent a prudent investment in this nation's youth, and the future contributions to the society and economy from those who are assisted by the program will multiply the return on this investment time and time again. Thomas Jefferson's observation that, "nothing more than education advances the prosperity, the power and the happiness of a nation" has stood the test of time, and is as relevant now as it was in his day. Indeed, it is the foresight of the leaders of past generations in providing for ever expanding educational opportunities that has provided much of the basis for the present richness of life and human achievements which prevail in this nation. Whatever problems and deficiencies may exist, let there be no mistake that this nation continues to surpass all others in terms of both the quality of life and contributions to human progress, due in large part to continuing emphasis on increasing educational opportunity.

This generation has had the benefit of an advanced society built on the foundation of expanding educational opportunities and increasing development of human resources. In return we have an obligation to invest in youth who will provide continuing advancement of the ideals and quality of this nation for future generations.

The relationship between development of human resources and future economic progress becomes more pronounced with each incremental step in achieving a more complex and sophisticated civilization and economic environment. The Sputnik era jolted the nation into recognition of the importance of education to national defense in a time of unparalleled technological complexity. Providing opportunity for every individual to achieve a full and productive life by developing his or her capabilities must continue to be a prime national goal.

This nation's past generations have made an enormous investment in development of a rich variety of public and private colleges and universities and postsecondary vocational institutions. This magnificent national resource provides an impressive array of educational opportunities. But opportunity without provision for realistic economic access to it is meaningless. And failure to provide the economic access which utilizes that great resource to the extent desired and deserved by the citizens of the nation would make these institutions nothing more than a hollow monument to the efforts of past generations.

Extensive utilization of the Program reflected by substantial volume indicates that the Guaranteed Student Loan Program has become a major national mechanism for providing economic access to postsecondary education. Moreover, the nature of the mechanism appropriately reflects the shared benefits from, and shared responsibility for, investment in the education. The program causes the individual who benefits directly from the educational experience to pay the cost. In recognition of the indirect benefits to the society at large, the society through the federal government provides the mechanism, including necessary subsidies, which permit the student to pay those costs from earnings after completion of the education.

Given the propriety of the investment in terms of future socio-economic benefits, and given the soundness of the program in allocating responsibility appropriately between the individual who benefits directly and the total society which benefits indirectly, attention to reduction of expenditures would seem appropriate only in view of a compelling force which requires curtailment of both providing individual opportunities for the nation's youth and developing the nation's human resources. Based on the recent federal budget reconciliation experience, it appears that the priority which has been assigned to increases in military expenditures and reductions in taxes may have become that compelling force.

This Committee and many other members of Congress are to be commended for courage in resisting inappropriate expenditure reductions on the Guaranteed Student Loan Program last session. This Committee also is to be commended for initiating these hearings in preparation for rational decisions in the midst of additional pressure for expenditure reductions this session.

IDENTIFICATION OF COST SAVINGS ALTERNATIVES

The attached discussion paper is an abbreviated and slightly revised version of a draft which was prepared last November in order to stimulate constructive attention to possible cost savings measures, should they once again become necessary. The paper contains three alternatives for reducing cost to the federal government of the Guaranteed Student Loan Program.

Each of the three alternatives addresses a different one of the three major expense areas of the program. The smallest of these expenses is the reinsurance reimbursement of claims for non-repayment of loans and the administrative cost allowance, which together serve as a subsidy reducing the price of insurance paid for by the student. The largest of these expenses is the special allowance payments to lenders which provide a reasonably competitive return to the lender while the student pays interest at less than market rate. The third expense, the size of which falls in between the other two, is payments of interest on the loan while the student is in school, thereby permitting postponement of repayment until after the education is completed and the student presumably is gainfully employed.

This testimony proposes a plan for your possible consideration which incorporates the first two alternatives described in the paper. The plan is not an ideal one. Indeed, as this Committee knows very well, opportunities for cost reduction in the Guaranteed Student Loan Program are virtually nil. Reduction in federal expenditures for the program must be achieved through one or the other (or a combination) of two undesirable alternatives:

(1) Reducing program volume which can be accomplished only by curtailing availability of loan funds, thereby curtailing access to postsecondary education, or

(2) Transferring more of the cost of the program from the federal government to other parties, particularly to student borrowers who are already in need or assistance.

CRITERIA FOR EVALUATING COST SAVINGS PROPOSALS

This and other plans for federal expenditure reduction must be evaluated in terms of some criteria which reflect policy objectives. The criteria (in priority order) which were used in selecting this plan for presentation and which are offerd to be considered for use in evaluating other plans are:

1. *Preservation of availability of and access to loan funds.*—This criterion emanates from the very purpose of the program and reflects the national commitment to developing the nation's human resources and to maximizing individual opportunity to achieve a satisfying and productive life by developing one's capabilities

through education. Cost reduction measures which would curtail access to loan funds either by limiting eligibility to borrow or by reducing available loan amounts below the amount needed to meet expenses would rank low on this criterion.

2. Preservation of accountability and incentives for sound program operation.—The Guaranteed Student Loan Program is a complex program involving a substantial amount of money. The fact that the funds for loans are provided from private capital rather than federal appropriations does not diminish the need for responsible program operation consistent with the total amount of money being utilized in the program. The complexity of the program has increased almost geometrically in recent years as the Congress has sought to modify the program to reduce federal expenditures in the context of increasing interest rates. Any program, which affects so many people and institutions, which involves such substantial capital from both public and private sources, and which is complex and growing in complexity, demands responsible administration.

Action which would lessen the capability of any of the parties involved in loans is self-defeating in terms of the long-range liability of the program. Under this criterion, a cost saving measure which reduced resources availiable to lenders and guarantee agencies below the amount necessary to insure responsible administration of the program would rank low. Similarly, a measure which enhanced accountability or incentives for sound administration of the program would rank high.

3. Preservation of program simplicity.—Given the complexity already built into the program, cost reduction measures which increase that complexity clearly are less desirable than those which do not, if all other things are equal. This criterion must be applied with caution because simplicity just for the sake of simplicity is not nearly so important as meeting needs. Accordingly, additional complexity might be preferable to more simple solutions which deny access to loans.

4. Preservation of low cost to users of the program.—This criterion has been ranked last, not because students are permitted to borrow at a lower price than is desirable, but because of the conviction that providing opportuntiy for students to borrow funds at a higher price is better then denying opportunity in order to keep the price low. Obviously, there is a point at which the price is sufficiently great as to be prohibitive and thus serves to deny opportunity. The price to the student of guaranteed student loan is not at that prohibitive level, and, while federal subsidies in amounts sufficient to perpetuate the present price are clearly defensible, increases in the current price would be less damaging than restricting access to funds. The ranking of this criterion suggests that, if the choice must be made, charging all students a higher interest rate would be preferable to arbitrarily limiting loan volume and hence denying opportunity for some students in order to keep the price low for others.

THE APPROACH TO ESTIMATING COST SAVINGS

In addition to reasonable criteria for evaluating cost saving measures, there must also be some reasonable approach to estimating the savings to be achieved. This is especially crucial for a program like the Guaranteed Student Loan Program, because the program is not one for which annual appropriation levels are useful in determining exenditures. Most of the federal expenditures for guaranteed student loans this year are not related to loans made this year. Rather, they are expenditure obligations already incurred on loans originated in previous years. Accordingly, the major portion of expenditures projected for next year cannot be affected by actions taken this year. The obligation for the expense already has been incurred.

Because the polices under which loans are made obligate the federal government for expenditures over several years, the most realistic approach to estimating the real impact of cost saving measures is to evaluate expenditures over the life of loans originated under the policies proposed. Otherwise, the Congress may institute a measure which generates savings for next year, but which is very costly as compared with alternatiave measures over the entire life of loans for which the federal government incurs an expenditure obligation.

ONE POSSIBLE COST SAVING PLAN

The following plan involves (1) elimination of the origination fee and replacing that fee with a change in the reinsurance formula which will generate greater savings over the life of loans originated than will the origination fee and (2) changing the interest rate and special allowance formula in a manner which reduces federal expenditures significantly during periods of high interest rates.

Elimination of origination fee and restructuring federal reinsurance

Under the present reinsurance arrangement, the federal government bears virtually the full cost of claims for non-payment of loans. This is the result of a reinsurance arrangement under which the federal government provides 100 percent reimbursement to guarantors on claims for death, disability and bankruptcy, and 100 percent of the first 5 percent of default claims each year, determined by comparing the dollar amount of defaults with the dollar amount of the original principal of all outstanding loans in repayment.

The proposed reinsurance arrangement, as described more fully in the attached discussion paper, would relate claims paid to the original principal amount of loans originated in the year in which the non-repaid loan was originated, and would obligate the federal government for partial reimbursement of claims, including death, disability, and bankruptcy claims, only after the claim rate reached 5 percent and for full reimbursement only of those claims occurring after the rate reaches 12 percent. The proposed arrangement would also involve elimination of the administrative cost allowance paid by the federal government to guarantors and would permit guarantors to charge an insurance premium adequate to cover both the cost of claims under the new reinsurance arrangement and essential operating expenses.

Estimated savings from the change in reinsurance are presented in Table I. With elimination of the origination fee, net savings for each $1,000 in new student loans can reasonably be expected to be approximately $18. Based on this estimate, the savings on an estimated $8 billion in loans made next year would be $144 million over the life of the loans. Assuming constant volume, an additional $144 million woud be saved on loans originated each year thereafter.

Although the proposed change would require an increase in the maximum guarantee fee of insurance premium paid by the student, the average maximum cost to the student would not be greater than current maximum authorized charges to the student with the origination fee, as demonstrated in the attached discussion paper. Hence, the $144 million savings would be achieved at no real expense to the student borrower.

The amount of savings derived from the change in the reinsurance arrangement could, of course, be increased by continuing the origination fee. Estimated savings with continuation of the origination fee would be approximately $68 per $1,000 in loans, or approximately $544 million on loans originated in a single year if annual volume is $8 billion.

The disadvantage of continuing the origination fee along with modification of the reinsurance arrangement is that the average maximum charge to the student would be increased by 5 percent of loan amounts. Accordingly, the objective should be to eliminate the origination fee with adoption of the proposed reinsurance arrangement, if possible.

The proposed reinsurance arrangement with elimination of the origination fee satisfies the proposed criteria for cost saving measures very well. Access to loan is not curtailed. Causing guarantee agencies to assume more financial responsibility for claims costs would enhance accountability of these agencies and would create a financial incentive for these agencies to keep defaults low. The present reinsurance arrangement, while theoretically offering such an incentive, provides no real financial motivation for the guarantor to perform effectively with respect to defaults until after the default rate has already gotten high.

The proposed reinsurance arrangement, combined with elimination of the origination fee, provides some simplification of the program. Adoption of the origination fee added an additional matter for lenders and the Department of Education to be concerned with in making interest subsidy and special allowance payments. It also added a factor in the program over which students often become confused and one which is not easily explained by lenders and student financial aid officers.

If adopted in connection with elimination of the origination fee, this proposal also satisfies the criterion of keeping the price to the student as low as feasible. If the origination fee had to be continued in order to preserve the program, students probably would reluctantly accept payment of additional 5 percent in order to have access to loans preserved.

Changing the interest rate and restructuring special allowance

Under the existing special allowance formula, the federal government bears the full burden of increases in program costs due to high interest rates. Federal special allowance payments vary directly with changes in the 91-day Treasury Bill rate without limitation. As described more fully in the attached position paper, the burden of cost increases due to high interest rates could be transferred to the student with modest risk to the lender by increasing the interest rate on student loans to 14 percent, establishing a constant special allowance rate of 4 percent and causing portions of the standard special allowance payment to be applied to repayment of principal when interest rates are low.

As indicated by the data presented in Table II, savings to the federal government from this proposed change would be substantial in periods of high interest rates. At a bond equivalent 91-day Treasury Bill rate of 12.5 percent, estimated savings would be $95 per $1,000 in loans originated over the life of the loan, or $570 million on $6 billion in loans originated in a year. At a Treasury Bill rate of 15.5 percent, the savings to the federal government increases to $240 per $1,000 in loans, or $1.4 billion on $6 billion in loans.

As indicated by the Table, this proposal does not generate savings when interest rates are low, and in fact would increase the cost to the federal government by $30 per $1,000 in loans when the Treasury Bill rate drops to 9.5 percent. Because it is when interest rates are high that the cost of the program to the federal government is high, absence of savings during periods of low interest rates when federal costs are lower anyway is not disadvantageous.

This measure for reducing federal expenditures during periods of high interest rates evaluates favorably in terms of the proposed criteria. The proposal does not limit availability of student loans. It does place an additional administrative burden on the lender, but provides compensation through a higher yield to the lender when the Treasury Bill rate does not exceed 12 percent and gives the lender assurance of a minimum yield of 14 percent compared with the current minimum yield of 9 percent.

The reduction in federal expenditures is accomplished primarily by transferring the cost of high interest rates to the student. Although the student would make repayments based on a 14 percent interest rate, the mechanism has the advantage of causing the actual cost to the student to be less when interest rates are lower through mechanism of applying an appropriate proportion of the constant special allowance to the principal reduction. This mechanism causes the actual cost (not the rate) of interest to fluctuate below 14 percent with prevailing short-term rates of interest. Thus, while the borrower makes repayments based on a constant rate, the actual cost fluctuates in the same direction as interest costs to other borrowers in the economy.

An alternative would be simply to increase the interest rate on student loans from 9 percent to perhaps 12 percent with the appropriate corresponding adjustment in the special allowance formula. Although a straightforward increase in interest rates has the advantage of initial simplicity, it could cause the rate charged on the loan to be higher than either desirable or necessary if interest rates decline. This situation could be alleviated by a provision which causes the rate on new loans to be lower when interest rates are low and rates on additional loans to be higher when interest rates increase. This arrangement, of course, exacerbates the problem of multiple interest rates for the program, and if rates continue to fluctuate, could cause some students to be paying rates which are higher than necessary for current market conditions and other students to be paying rates which are lower than necessary in view of prevailing market conditions.

On the other hand, a simple change in interest rates might be preferred by lenders wishing to protect an unlimited yield on student loans. The proposal advanced here does have the disadvantage of an 18 percent maximum rate to the lender. This is at least partially offset by the higher minimum yield and the .5 percent increase in yield when the T-Bill rate is between 10 and 14 percent.

It should be emphasized that the plan presented here is not advanced as an ideal proposal, although the component of the plan involving restructuring of the reinsurance arrangement and elimination of the origination fee has merit as an improvement to the program whether or not additional savings of federal expenditures are required. Hopefully, the total plan is useful in providing additional perspective and ideas on how any required expenditure reductions might be achieved responsibly.

COMMENTS ON OTHER COST SAVINGS MEASURES

As is apparent from the priority ordering of the recommended criteria for evaluating expenditure reduction measures, you are urged to view very cautiously any proposals which would limit availability and access to loans for students. This would include proposals for arbitrary limits such as a maximum number of loans in each state and any proposals to curtail the yield on student loans to commercial lenders sufficiently to diminish their active participation in the program.

Any proposal to diminish the opportunity for statewide last resort lending and secondary market organizations to issue tax exempt revenue bonds to obtain funds for student loans should also be rejected because of the devasting impact which such proposals would have on the availability of student loans in approximately twenty states. The ability of the commercial lending community to meet the total need for loans varies dramatically from one state to another. In states which serve as major money centers, commercial lenders may very well be able to meet the total need within the state and some need in other states as well. On the other hand, states which are not major financial centers badly need the back-up capability which comes from participation of statewide last resort lending and secondary market organizations financed with tax exempt revenue bonds. Moreover, the loss of federal revenue throught the tax exemptions is counter-balanced by the lower special allowance payments made to organizations with tax exempt financing.

Also to be adopted only as a last resort should be any proposals which both restrict borrowing capacity of students and increase costs to lenders. An example would be a proposal to extend the new needs analysis and expected family contribution provisions to students from families below the $30,000 annual income level.

The expected family contribution provision tends to reduce average loan size which increases cost to the lender of loan servicing as a percentage of loan principal. Meeting the total borrowing needs of a student though two loans—one from the Guaranteed Student Loan Program and one from the auxiliary or PLUS program—is twice as costly for the lender as meeting that same need with a single guaranteed loan. In addition, the "expected family contribution" provision complicates the origination process, extends the time period for originating loans, places additional burdens on educational institutions, and makes financial planning for postsecondary education more difficult for the student due to uncertainty over borrowing capacity prior to receipt of the needs analysis results. It is questionable that the savings from extending the expected family contribution requirement below the $30,000 income level are adequate to compensate for the additional problems created by such a requirement.

IMPROVEMENT OF AUXILIARY OR PLUS PROGRAM

The effort to shift borrowing from guaranteed student loans to less heavily subsidized auxiliary or PLUS loans would be facilitated by three changes.

1. Either the student or the parent should be permitted to borrow under PLUS in order to preserve borrowing capacity when the needs analysis yields an expected family contribution but borrowing by the parent is not considered feasible by the lender or the parent (e.g., the parent needs to preserve borrowing capacity for another purpose or the parent has a poor credit rating).
2. The parent should be permitted to co-sign for the student borrower of a PLUS loan for the interest payments while the student is in school without being obligated for repayment of loan principal (this will assist students whose parents are willing to commit enough of their borrowing capacity to cover inschool interest, but are reluctant to commit an amount equal to the principal for an extended repayment period).
3. The special allowance formula in PLUS loans should be adjusted to provide a gross yield to the lender of the T-Bill rate plus 4 percent, rather than plus 3.5 percent, in order to stimulate lender participation in light of the relative higher cost of originating and servicing PLUS loans.

TABLE I.—FEDERAL EXPENSE FOR CLAIMS PAYMENTS OVER LIFE OF GUARANTEED STUDENT LOANS PER $1,000 IN LOANS ORIGINATED

Default rate [1]	Current formula [2]	Proposed formula	Savings on claims	Elimination of administrative cost allowance	Gross savings	Elimination of origination fee	Net savings per $1,000
5 percent	$60	$8	$52	$10	$62	($50)	$12
10 percent	110	50	60	10	70	(50)	20
15 percent	157	99	58	10	68	(50)	18
20 percent	205	149	56	10	66	(50)	16

[1] Default rate refers to the percent of loan proceeds guaranteed in a single year which go into default at any time. (If, of $1,000,000 in loans guaranteed in 1 year, defaults eventually occur on $100,000, the default rate is 10 percent,) Claims for death, disability, and bankruptcy are not included in default rate, but are included in expense estimates at the rate of 1 percent over the life of a loan portfolio.

[2] Estimates indicated for 15 and 20 percent rates assume that some portion of defaults are not reimbursed. Because reimbursement under the current formula is affected by how defaults of loans guaranteed in 1 year are distributed over time and the volume of loans in repayment from other years, all defaults at the 20 percent rate actually may be eligible for full Federal reimbursement.

TABLE II.—ESTIMATED FEDERAL EXPENSE PER $1,000 FOR SPECIAL ALLOWANCE AND INTEREST SUBSIDY OVER LIFE OF GUARANTEED STUDENT LOANS [1]

91-day T-bill rate [2]	Special allowance formula		Savings
	Existing [3]	Proposed	
9.5 percent	455	485	−30
12.5 percent	628	533	95
15.5 percent	801	561	240
18.5 percent	975	561	414

[1] Reference is to each $1,000 in loans made in the program. Calculations assume 2 years in school, a 6-month grace period, and a 7-year repayment schedule with 20 percent of each $1,000 in loans being originated or purchased and held by a tax-exempt holder.

[2] Bond equivalent rate.

[3] Does not include allowance for origination fee which would reduce all amounts by $50 each, if continued. Assumes that 20 percent of loans made are either originated or purchased by tax-exempt holders.

DISCUSSION PAPER

(By Richard C. Hawk)

This paper contains three alternatives for reducing federal expenditures for the Guaranteed Student Loan Program. Each of the alternatives would generate significant savings and the savings from all three would be greater than necessary or desirable.

These alternatives are presented as viable substitutes for the cost saving measures which were adopted in the summer of 1981. Those changes, which were conceived as budget reduction measures under the severe pressures and time constraints of the budget reconciliation process, reflect the lack of opportunity for adequate deliberation and judgment. They generally are not sound social policy when viewed as anything other than temporary expediences to achieve immediate savings. The ideas presented in this paper demonstrate that adequate savings can be achieved through more constructive changes than those adopted in the summer of 1981.

Any proposal to reduce federal expenditures for the Guaranteed Student Loan Program requires either increasing costs or risks to other parties (students, lenders, education institutions, guarantee agencies), or reducing loan dollar volume by restricting opportunity. The alternatives presented in this paper reflect the premise that the needs of both students and the society are better served by preserving opportunity at a higher price than by restricting opportunity in order to keep the price low.

Accordingly, each of the three alternatives has been designed to achieve savings without restricting opportunity for students to borrow funds needed to meet postsecondary education expenses. Three alternative mechanisms are proposed that transfer cost from the federal government to other parties, particularly recipients of loans. This is consistent with the view of some that the need to reduce the federal budget requires the shifting of some costs of federal programs to the beneficiaries of the service provided.

The three alternatives in preferential order are:

1. Reduce federal cost for default and other claims by restructuring federal reinsurance on student loans and eliminate the administrative cost allowance, paid to guarantee agencies.
2. Eliminate unpredictability and the high cost of federal special allowance payments during periods of high interest rate by shifting some of the risk of fluctuating interest rates to students and limiting the special allowance to 4 percent.
3. Reduce the cost of the in-school interest subsidy by relying on grants for the first year of undergraduate education and loans for the last year of undergraduate education.

Each alternative is discussed in detail in this paper.

ALTERNATIVE 1

FEDERAL SAVINGS THROUGH MODIFICATION OF REINSURANCE AND ELIMINATION OF ADMINISTRATIVE COST ALLOWANCE

The existing reinsurance arrangement causes the federal government to bear the full cost of virtually all claims for nonpayment of loans by the borrower. The federal government reimburses the guarantee agency for 100 percent of the amount of claims paid due to death, disability and bankruptcy. The federal government also reimburses the guarantor for 100 percent of the first 5 percent of default claims paid each year, with the percentage of defaults determined by comparing defaults which occur during the year with outstanding loans in repayment during the year.

The effect of the current reinsurance arrangement is to cause the federal government to stand the cost of claims as if it were the primary or even the only insurer of student loans. This major cost could be eliminated if the reinsurance were reconceived as protection against disaster, with initial default costs paid by the guarantee agency without reimbursement.

Elements of this proposal are:

(1) Eliminate 100 percent reimbursement of claims due to death, disability and bankruptcy.

(2) Eliminate present reimbursement formula under which federal government pays 100 percent of the first 5 percent of defaults each year, 90 percent of the next 4 percent and 80 percent of all defaults thereafter.

(3) Substitute a new reimbursement formula to be applied to individual loan portfolios over the life of each portfolio, with a portfolio consisting of all loans guaranteed in one year. The new rates of reimbursement for claims (including default, death, disability and bankruptcy) on each loan portfolio should be:

Federal reimbursement rate (percent)

Claims as percent of portfolio:	
0 to 5	0
5 to 9	80
9 to 12	90
Over 12	100

(4) Eliminate federal administrative cost allowance paid to guarantee agencies presently authorized in the amount of 1 percent of all loans guaranteed each year.

(5) Provide for a guarantee fee or insurance premium sufficient in amount to replace the administrative cost allowance and to provide for sufficient reserves to cover increased risk to the guarantor. The maximum non-refundable guarantee fee under current regulation is 1 percent per year for the in-school period of the loan plus one year. Adoption of the proposed reinsurance structure and elimination of the administrative cost allowance will require authorization for a non-refundable guarantee fee of 2½ percent plus 2 percent per year for the in-school and grace period of the loan.[1]

Savings to the federal government will be approximately 1 percent of the amount of loans originated each year plus 100 percent of the first 5 percent of defaults, 10 percent of the next 4 percent of defaults, and 100 percent of claims for death, disability and bankruptcy minus 10 percent of defaults between 9 and 12 percent, and 20 percent of all defaults over 12 percent. Savings will actually be greater because under the present forumula the default rate is cumulative only within a year, whereas the proposed modification would cause the claims rate to accumulate over the life of the portfolio.

DISCUSSION OF ALTERNATIVE 1

Alternative 1 increases the liability of loan guarantee agencies and transfers some of the cost of insuring student loans from the government to student borrowers. Because the change affects only the borrower and guarantee agencies, education institutions and lenders would not be affected. Consequently, the changes could be accomplished easily.

Transferring additional insurance cost from the government to the borrower can be justified on the basis that neither the present nor the proposed guarantee fee is sufficient to cover the cost of insurance, which is (a) as broad as the student loan guarantee, (b) granted on a non-discriminatory basis and (c) covers an uncertain period of time, extending as long as fifteen years. The proposed change also can be justified on the basis that the purpose of federal reinsurance should be to provide protection against a disastrous situation in order to maintain private funding sources to remain committed to making student loans. Federal reinsurance should be provided by the government at government expense. A self supporting non-reinsured portion of the total insurance liability could be borne by borrowers. The present reinsurance arrangement does much more than serve as protection against unmanageable losses due to a disastrous situation. It serves as a subsidy which permits the guarantee fee or premium charged to the borrower to be low.

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[1] An alternative would be a non-refundable fee of 1½ percent per year on the anticipated amortized principal outstanding, assuming a five year repayment period.

The administrative cost allowance also serves as an indirect subsidy to the borrower. By covering some of the administrative costs of guarantee agencies which insure loans, the administrative costs allowance reduces the amount which agencies must charge the borrowers as insurance premiums or guarantee fees.

Although a good case can be made for subsidizing the Program as heavily as possible to keep student costs low, benefits of the Guaranteed Student Loan Program probably would not be significantly diminished with an arrangement under which federal reinsurance serves primarily as protection against disaster rather than as an indirect subsidy of insurance premiums. Moreover, as demonstrated by the data below, adoption of Alternative 1 with the necessary increase in the guarantee fee would result in no increase in the average permissible charges to students if the 5 percent origination fee were eliminated.

COMPARISON OF CURRENT AND PROPOSED CHARGES TO STUDENTS PER $1,000 OF LOAN PRINCIPAL [1]

Year in school	Current charge [2]	Proposed charge [3]
Freshman	$95	$115
Sophomore	85	95
Junior	75	75
Senior	65	55
Average [4]	80	85

[1] Amounts are approximate.

[2] Includes 5-percent origination fee and guarantee fee at rate of 1 percent per year in school and 6 month grace period.

[3] Based on no origination fee and guarantee fee of 2.5 percent plus 2 percent per year in school and 6 months of grace period.

[4] Average charge per $1,000 assuming loans in equal amounts for each year of undergraduate education.

It should be noted that the need for an increase in the guarantee fee under the proposed reinsurance arrangement is very real. Although the theoretical exposure to guarantee agencies is higher under the existing reinsurance arrangement than it would be under the proposed change, the actual exposure is greater under the proposal as evidenced by the actual default experiences of agencies.

Under the existing arrangement, guarantee agencies never suffer a loss until defaults exceed 5 percent in any year. At the beginning of each year the slate is wiped clean and the agency is once again fully protected against the first 5 percent of defaults. In addition, the federal government stands the cost of all claims for death, disability, and bankruptcy.

Under the proposed arrangement, guarantee agencies would always stand the loss on the first 5 percent for defaults as well as for death, disability, and bankruptcy. Accordingly, conditions of the proposed arrangement will require deposits to reserve funds of approximately 6 percent for each loan guaranteed. Reserve fund deposits under the present arrangement normally are less than 2 percent.

ALTERNATIVE 2

FEDERAL SAVINGS THROUGH CHANGE IN SPECIAL ALLOWANCE

Under existing law, the federal government absorbs the cost of high interest rates by paying a special allowance, the amount of which varies with the 91-day T-Bill rate. In addition to causing dramatic increases in federal costs for the Program during periods of high interest rates, the present special allowance arrangement causes costs to the federal government to be unpredictable. Greater predictability and substantial savings during periods of high interest rates can be achieved by transferring the risk of fluctuating interest rates to students and lenders. The elements for the proposal to achieve this objective are:

(1) Increase the interest rate charged to students during the repayment period of loans from 9 percent to 14 percent.

(2) Set the amount of the federal special allowance payment by the federal government to lenders on repayment loans at 4 percent.

(3) Permit the interest cost (not rate) to students to vary below 14 percent according to fluctuations in general interest rates for loans in repayment by applying a varying portion of the special allowance to principal repayments when the 91-day T-

Bill bond equivalent rate drops below 10 percent. The amount applied to the principal shall be the portion of special allowance remaining after determination of the amount of special allowance to be used as a supplemental interest subsidy. The percentage of the special allowance to be retained by the lender as interest shall be determined by subtracting 10 from the quarterly average bond equivalent 91-day T-Bill rate and dividing by 4 (T minus 10 divided by 4 = interest subsidy).

(4) Require portions of the quarterly special allowance payment applicable to principal reduction to be credited to the loan account only on the last day of each fiscal year or on the date a loan is repaid in order to avoid prohibitive loan servicing cost.

(5) Provide special allowance payments on repayment loans, i.e., loans in the repayment phase, from tax exempt funds only in the amount determined to be used as principal reduction according to the formula above.

(6) For interim loans (loans on which the borrower has not yet entered a repayment phase) held by commercial lenders, provide special allowance payments only in the amount determined to be applied to interest according to the formula above and provide no special allowance payments on interim loans from tax exempt dollars.

The effect of these changes will be (a) to reduce federal special allowance payments to a constant 4 percent for repayment loans held by commercial lenders, (b) to a varying amount which cannot exceed 4 percent on interim loans held by commercial lenders, (c) to a varying amount which cannot exceed 4 percent on repayment loans for tax exempt funds and (d) to zero on interim loans made from tax exempt funds. Students will benefit because actual interest costs can be less than 14 percent by reducing loan principals when T-Bills fall below 10 percent. The effect for lenders will be revenue (interest plus special allowance) from student loans in an amount which varies between 14 percent and 18 percent, accompanied by an increase in the rate of return of .5 percent over the current return on loans.

DISCUSSION OF ALTERNATIVE 2

Under existing law the cost of interest to borrowers can never exceed 9 percent on student loans regardless of prevailing interest rates. Under Alternative 2 the cost of interest will vary with prevailing rates and could be as high as 14 percent.

This alternative transfers risk of fluctuating interest rates from the federal govenment to students (and partially to the lender) without imposing the complexities and uncertainties of a variable interest rate on students. Students would obtain loans with the understanding that monthly repayments will be lower prevailing interest rates when portions of a standard 4 percent special allowance is credited as principal repayments when loans are in the repayment phase. If interest rates decline, annual principal reductions from the special allowance will cause the loan to be repaid more quickly and the actual cost of interest of students will decline, even though the rate remains at 14 percent. The government will benefit from declining interest rates because more rapid repayment of the loan will shorten the period of time for which the government stands the expense of the special allowance.

Advantages to the government are great. First, the cost of the Guaranteed Student Loan Program would be considerably more predictable, and, second, the government cost for special allowance would be reduced to a constant 4 percent on repayment loan held by commercial lenders and to a rate which can fluctuate below 4 percent on interim loans held by commercial lenders and on repayment loans acquired with tax exempt funds. The special allowance is completely eliminated for interim loans acquired with tax exempt funds.

Although students continue to benefit from predetermined constant interest rate, and although students benefit from declines in prevailing interest rates, the cost of interest to students necessarily will be higher than the present 9 percent cost. It should be noted that the increase in cost would not affect the borrower while the borrower is a student. Federal interest subsidy payments to commercial lenders would continue while students are in school. Borrowers will experience an increase in costs after completing their education and presumable becoming situated in an income producing endeavor.

This alternative has advantages and disadvantages for the lender. Return to lenders on student loans would no longer be unlimited. For commercial lenders the maximum return would be 18 percent. On the other hand, the mimimum return to lenders would be increased from 9 percent to 14 percent. Moreover, the rate of return to lenders would be increased from T-Bill plus 3.5 percent to T-Bill plus 4 percent. In other words, the disadvantage of an 18 percent maximum return would be balanced by the advantages of a 14 percent minimum and a .5 percent increase in the amount by which the return exceeds the 91-day T-Bill rate. Lenders would fare better under the alternative when interest rates are at a level which under the present formula would produce a return of 17½ percent or less. Lenders would fare less well under the proposal when interest rates are sufficiently high to cause the return on student loans under the present formula to exceed 18 percent.[2]

Under this alternative, lenders also would be disadvantaged by the administrative complexity of allocating a portion of the standard quarterly special allowance payment on loans in repayment to principal. The burden of this provision can be reduced by requiring that the portion of special allowance payments to be applied to principal be credited to the loan account only on the last day of the fiscal year or on the date the loan is fully repaid. Such a mechanism also will permit the lender to have some "float" as partial reimbursement for this administrative task.

ALTERNATIVE 3

FEDERAL SAVINGS THROUGH REDISTRIBUTION OF GRANTS AND LOANS

Because the Federal Government pays interest on guaranteed student loans while students are in school, loans to freshmen are more expensive than loans to seniors. On the other hand, the federal cost of grants to students is the same for all students. Accordingly, significant savings can be achieved by reallocating grant funds which increases expenditures for grants to freshmen and eliminates grants to seniors, with a corresponding elimination of loans to freshmen and an increase in loan amounts to seniors. This can be accomplished without reducing total assistance (grants and loans) provided to students and additional savings can be achieved by discounting interest (and eliminating federal interest subsidy payments) for loans on which the in-school period will be one year or less.

Elements of the proposal to achieve savings through reallocation of grants and loans are:

(1) Eliminate guaranteed student loans for the first year of undergraduate postsecondary education except for students in one year programs.

(2) Make guaranteed student loans available to first year students in one year programs without an in-school interest subsidy by requiring that interest on the loan for the in-school period of the loan plus the six month grace period be discounted from loan proceeds at the time of loan origination.

(3) Continue subsidized loans (loans on which the interest is paid by the federal government while the student is in school) in accordance with existing terms and conditions of the Guaranteed Student Loan Program for undergraduate students in the second and third year of postsecondary education.

(4) Continue Pell grants for first, second and third year undergraduate students in accordance with existing conditions and requirements, with a 75 percent increase in the funding for first year students.

(5) Eliminate grants for students in the fourth year of undergraduate postsecondary education.

(6) Make guaranteed student loans available to fourth year undergraduate students of up to $5,000 on a nonsubsidized basis by requiring that interest for the period of the loan and the 6 month grace period be discounted from the proceeds of the loan at the time of loan origination.

Substantial savings to the federal government will be achieved. Savings will be equal to (1) costs associated with all loans to first year students except students in one year programs, (2) interest subsidy payments for first year students in one year programs, and (3) interest subsidy payments on loans to fourth year undergraduate students.

DISCUSSION OF ALTERNATIVE 3

Alternative 3 is the only one of the three proposals which would require changes to programs other than the Guaranteed Student Loan Program. This altenative recognizes that the federal effort in student financial assistance is broader than loans and that changes in one student assistance program can appropriately be considered in conjunction with changes to another as part of policy development for the total student assistance effort.

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[2] The disadvantage (to the lender) of the 18 percent maximum return could be eliminated by permitting a deduction for additional interest from the next monthly principal repayment after each quarterly special allowance payment in the amount necessary to assure that the return to the lender is equal to the prescribed amount over the 91-day T-Bill rate. The effect of this modification would be to cause the repayment period to be extended by the number of repayments necessary to make up for application of principal repayments to interest. With this modification the return to the lender should be continued at T-Bill plus 3.5 and not increased to T-Bill plus 4. The formula would become T-Bill minus 10.5 divided by 4. Obviously, this advantage to the lender would be gained at the expense of students who would be required to asme greater risk with respect to increases in interest rates.

One reason for previous increases in the total federal expenditures for student assistance is that, at least at the undergraduate level, the Federal Government has attempted to make all forms of assistance available to students throughout the period of education. Alternative 3 seeks to enhance the efficiency of the federal investment in student assistance by relying essentially on grants for the first year of undergraduate education, on a combination of grants and loans for the second and third years, and on loans exclusively for the fourth year. Savings are generated because the cost of a grant remains the same regardless of the school year which the grant is used to support, while the cost of a loan varies significantly with the number of remaining years in school at the time of origination, due to the in-school interest subsidy.

In general, use of grants at the beginning of postsecondary education and loans nearer the end of postsecondary education is reasonably sound policy if appropriately structured. Grants represent a more powerful instrument for stimulating entry into postsecondary education than loans. Loans are more comfortably utilized by students as they progress through postsecondary education because each additional year enhances confidence that they will complete their educational program successfully and earnings to repay the loan are in sight.

Eliminating loans for first year students in four year programs could create serious problems for some individual students if increases in grant funds for first year students are not as great as the amounts of loans eliminated. Should sufficient grant funds not be available students with marginal need (those without sufficient demonstrated need to qualify for a grant) would be left out in the cold with neither a grant nor a loan.

Under Alternative 3 additional savings would be generated through elimination of the interest subsidy on loans to first year students in one year programs and to all loans to students in the last year of undergraduate education. The result would be a savings on in-school subsidy payments of approximately 50 percent. Achievement of this savings to the government would, of course, be at the expense of increased costs to the borrower.

CONCLUDING REMARKS

Each of the three areas of federal cost for the Guaranteed Student Loan Program is addressed by one of the alternatives presented in this paper. The cost of the indirect subsidy of insurance premiums through the administrative cost allowance and highly favorable reinsurance provisions is addressed by Alternative 1. The cost of the special allowance is addressed by Alternative 2, and Alternative 3 reduces the cost of the in-school interest subsidy on loans. Substitution of any one of these alternatives for the family contribution and origination fee provisions adopted in the summer of 1981 would be advantageous.

Obviously, there are differences in the ease with which reductions can be achieved among the three cost areas. Altenative 1 is most easily implemented of the three alternatives and is least disruptive to the program.

These alternatives are intended to stimulate constructive thinking on how responsible action can be taken to achieve federal cost reductions while preserving major benefits of the Guaranteed Student Loan Program and achieving sound social policy objectives. Adoption of one or more of these alternatives would not preclude utilization of other temporary cost saving measures to meet budget objectives in a single year. However, such stop-gap measures should not be considered as a substitute which reflect a balance in due consideration for cost and for social policy objectives.

In addition to generating significant savings for the federal government, adoption of Altenative 1 would provide opportunity to provide additional borrowing capacity for students through non-subsidized loans at virtually no cost to the federal government. Availability of non-subsidized loans in adequate amounts under the Guaranteed Student Loan Program would eliminate the need for establishment of a multiplicity of separate loan programs which are being proposed to counteract loss of funds due to reductions in federal student assistance programs.

Mr. SIMON. Dr. Delores Cross, president of the New York State Higher Education Services Corp.

We are pleased to have you here with us, Dr. Cross.

STATEMENT OF DOLORES E. CROSS, PRESIDENT, NEW YORK STATE HIGHER EDUCATION SERVICE CORP.

Dr. Cross. Thank you, Chairman Simon, and members of the subcommittee.

I would like to discuss issues and preliminary requirements in the survey that we have conducted in New York and share with you some of my concerns as they relate to Federal cutbacks in student financial aid.

New York State students receive more financial aid than students in any other State, either per capita or in absolute dollars.

The New York State Higher Education Services Corp. administers New York's grants, scholarships and loan programs.

Additionally, the corporation coordinates the State's programs with those of other levels of local, State and Federal government.

Thus, the corporation is deeply involved in New York State's commitment to higher education as a growth and service industry for its citizens.

The State's postsecondary enrollment is about 9 percent of the national enrollment of 11 million. The State's students receive close to 14 percent of the Federal financial aid dollar.

New York itself will provide, in 1982–83, $327 million in grant and scholarship aid to resident students, representing almost one-third of the national total for all States.

In sum, the higher education industry is of profound importance to the State—and that importance is most easily measured in terms of enrollments and financial aid to students.

As a result of the unprecedented dependency of college students on financial aid, the corporation initiated a comprehensive survey to determine how all postsecondary students in New York State finance their education; that is, how they package personal and external resources to meet their educational costs.

At a time when the Federal Government proposes changes in financial aid that will alter the very nature and philosophy of higher education, this survey will enable the State to plan effectively to meet these challenges.

To date, New York is the only State to attempt such a survey.

Yet, we are working with other organizations and our colleagues and looking at research in many areas. Among the questions to which we hope to find answers are:

How do students from various backgrounds and at various institutions pay their costs of attendance?

How will students be affected by changes in financial aid programs?

How are students likely to "react" to changes in financial aid programs?

How can the State move to deal with "pockets" of unmet present or future financial need among the college-going citizens?

This survey may be unique because we are not looking only at students who are receiving financial aid but also students who are nonaid recipients.

Preliminary findings from the Pilot indicate that graduate students and enrollees at proprietary institutions such as nursing and business schools are very concerned about possible financial aid reductions since major portions of their aid are provided by guaranteed student loans and Pell grants, both Federal programs.

City utilization of Pell grants may be as high as 80 percent. GSL in the private sector is as high as 40 percent and slightly higher in the State university system.

When one looks at the State university system, in 1979 their utilization of the guaranteed student loan was approximately 16 percent. Undergraduate utilization of TAP, that is the State's tuition assistance program, is approximately 50 percent.

The survey tells us that the income profile that would be the most affected are those that are in the lower to middle income tax bracket and that the cutbacks in the GSL may have an additional proportionate impact on those students who are attending low-cost community colleges in both the public and the private sector. The survey will tell us who will be affected by the program.

At the current time we have completed the pilot study. The pilot study included 30 colleges with approximately 800 students. These results will be presented to our trustees next week as well as to a committee of presidents and will be shared with the postsecondary committee.

The complete statewide survey will include 300 institutions and over 4,000 students.

The results of this survey we expect to have available to our colleagues in other States and you as members of the Subcommittee on Postsecondary Education as well as policymakers throughout the State.

We will, therefore, be using our findings to satisfy both the State of New York and the Federal Government in the distribution of financial aid.

We believe these data will enable both entities to plan effectively to meet student financial aid needs at the postsecondary level in New York State and the Nation.

The development of rational responses to Federal cutbacks and our ability to respond and counter additional proposals demand a period of stabilization, a period in which States and the Federal Government can examine the data and think things through.

It also demands that we can examine some deeper questions in terms of how will the effects of the cuts be distributed? How will the effects impact different regions?

How will these cutbacks interact with already identified demographic and enrollment changes?

While meeting these challenges we must continue to keep the purposes and objectives of financial aid clearly in mind. That is to provide access by removing financial aid barriers and promoting choice of institutions based on talents and career objectives rather than costs.

This period of program retrenchment brings with it a range of administrative challenges including adapting our processing systems to program changes quickly and efficiently so that timely notification and distribution of aid is available.

This is particularly important in a period of instability. It also requires that we work with lenders to initiate new programs.

As my colleagues have testified, this is not an easy task. In New York City we have only been able to identify four banks at the present time who are willing to accept ALAS loans.

We are very concerned about the criteria that some banks seem to be setting up as it relates to the PLUS money, criteria that are in some cases beyond what the Federal Government requires or what the corporation may require. We have to examine that and look at that as it relates to the status of those banks and their participants.

We are also working on developing and creating innovative systems of communication, communication to students and to parents and to colleges about the changes in the regulations and the impact of these cuts.

In sum, as we look at the data, New York, as a result of the current changes, will lose approximately $275 million in student financial aid. The loss means that every student who receives some form of financial aid will have an average loss of $850.

If the cutbacks that have been proposed for the GSL at the graduate level are to occur this will impact on approximately 85,000 students and increase the loss in student financial aid dollars in New York to over $350 million.

We are concerned, we appreciate this opportunity to discuss with you a process that we are taking to help you and help the State of New York and other States think things through.

We view higher education as an industry, a service industry and a growth industry that impacts upon the growth of other industries.

In my work in New York the concern has been what will be the impact of the cuts? What is the interaction of the various student financial aid programs, will there be a period of stability in which we can compare the data, look at what may happen to higher education as an industry and also take time to see what the changes mean to the quality of life for New Yorkers and the Nation?

[The prepared statement of Dolores Cross follows:]

Prepared Statement of Dolores E. Cross, President, New York State Higher Education Services Corp.

New York State students receive more financial aid than students in any other state, either per capita or in absolute dollars. The New York State Higher Education Services Corporation administers New York's grants, scholarships and loan programs. Additionally, the Corporation coordinates the State's programs with those of other levels of local, State and federal government. Thus the Corporation is deeply involved in New York State's commitment to higher education as a growth and service industriy for its citizens.

The State's postsecondary enrollment is about 9 percent of the national enrollment of 11,000,000. The State's students receive close to 14% of the federal financial aid dollar. New York itself will provide, in 1982-83, $327 million in grant and scholarship aid to resident students, representing almost one-third of the national total for all states.

In sum the higher education industry is of profound importance to the State—and that importance is most easily measured in terms of enrollments and financial aid to students.

As a result of the unprecedented dependency of college students on financial aid, the Corporation initiated a comprehensive survey to determine how all postsecondary students in New York State finance their education; that is, how they package personal and external resources to meet their educational costs. At a time when the federal government proposes changes in financial aid that will alter the very nature and philosophy of higher education, this survey will enable the State to plan effectively to meet these challenges. To date, New York is the only state to attempt such a survey.

Among the questions to which we hope to find answers are:

How do students from various backgrounds and at various institutions pay their costs of attendance?

How will students be affected by changes in financial aid programs?

How are students likely to "react" to changes in financial aid programs?

How can the State move to deal with "pockets" of unmet present or future financial need among the college-going citizens?

It must be noted that all other state surveys have used financial aid recipients as the population; that is, they have ignored those who pay their own way from family and personal resources only. The New York survey will enables the Corporation to compare the financial profiles of aid recipients to those of non-aid recipients.

Preliminary findings from the Pilot indicate that graduate students and enrollees at proprietary institutions such as nursing and business schools are very concerned about possible financial aid reductions since major portions of their aid are provided by Guaranteed Student Loans and Pell Grants, both federal programs.

The Survey will tell us who in the State will be affected by various federal program cuts. Moreover that effect will be focused by income level and institutional type. By factoring in student attitudinal data, the Survey may give indications of consequent student behaviors with aid shortfalls over various income levels and institution types.

The Corporation will use its findings to assist both the State of New York and the federal government in the distribution of financial aid. We believe these data will enable both entities to plan more effectively to meet student financial aid needs at the post-secondary level in New York State and the nation.

It seems useful here to indicate some of the major questions which will shape our final research design:

How is federal student aid distributed in New York?

a. which students and which institutions benefit most from guaranteed loans?

b. which from Pell grants?

c. which from campus-based programs?

How is federal aid distributed over various income levels and regions of the State?

What fraction of real college going cost does federal aid cover?

Given various scenarios of federal financial aid cutbacks, the Corporation will need to consider deeper questions:

How will certain financial aid cutbacks affect institutions?

How will the effects be distributed over various sectors and income levels?

Will there be acute regional difficulties caused by the cutbacks?

Will certain types of institutions within sectors have more difficulty in addressing changes than others?

How will these cutbacks interact with already identified demographic and enrollment changes?

How can institutions best plan for the dislocations implied by the federal cutbacks?

Mr. SIMON. Thank you, Dr. Cross.

Is there any possibility the survey you are talking about can be speeded up? We are in the process that we are going to be making some decisions that are going to make that survey almost meaningless within the next couple of months.

Ms. CROSS. In my very slim documents I just shared with you what the survey is looking at, next week we will have the results of our preliminary.

I was asked to share the first with the board of trustees and the committee of presidents and it should be available in your hands by the end of next week; the complete survey, that is the pilot.

We use that pilot to look at our processes in terms of sampling techniques and also to rework various aspects of the survey.

Mr. SIMON. How soon will this pilot reach us?

Ms. CROSS. The pilot will be available to you at the end of next week.

Mr. SIMON. What about the other survey?

Ms. **Cross**. Our time line is the end of March and early part of April.

Mr. **Simon**. The more you can press on time on that the more helpful, frankly, it is going to be here at the Federal level.

Dr. Cronin, I regret that I was not here for your testimony.

What happens on the parent loans where you say in your testimony more than 95 percent of the applicants prove to have satisfactory credit ratings and capacities and so forth.

What about the other 5 percent?

Mr. **Cronin**. If they feel, Congressman, that they have been unfairly treated and discriminated against they have access under the Equal Credit Opportunity Act to protest and we have been waiting to find out if that is going to happen. It has not.

In most instances, the families are counselled and realize that the information they have provided to the bank shows that they do not have the capacity to repay those loans and, therefore, the program cannot serve them.

And there may be a need, therefore, for the student to work an additional few hours a week or to be considered for other campus-based programs if the family is truly hard up.

Mr. **Simon**. Are you finding that those 5 percent, my guess is that they may be among the students who need the help the most.

Are those students then just skipping college? Are they rearranging the work schedule as you suggest or has there been any follow-up on that?

Mr. **Cronin**. We have not had any survey of those families. One of the ironic commentaries we could make is that some of the families, in order to qualify for student aid go into the college and show how poor they are. They show that they have got debts coming out their ears, the number of monthly payments they have on the house and on the automobile and everything else, there is no way that they can do anything but apply for another grant or scholarship from the college.

Unfortunately, some of these families have then taken the identical documents and shown this to a bank to qualify for a PLUS loan. Well, a PLUS loan is really a middle-income device because the way it is written you have got to go into repayment within 60 days. You have got to have enough cash not tied up to make a $50 repayment.

So using these documents to show how poor you are on campus does not go over very well at the bank.

It could be that in some cases the families have not shown us all the resources because in at least a couple of instances that we have heard about anecdotally, people say, all of a sudden I realize I have got to have some money to repay, let's go back and take a look at the assets again, maybe I can qualify.

The truth is that in the first 12 months we really have not had enough time to do a detailed survey of what happens to the 3 or 4 percent who have been denied. That estimate comes from the largest bank in the program and we, frankly, have been surprised we have not heard more concerns either from those families or from the students or the college aid officers. So apparently they have been able to get credit elsewhere or else other forms of student aid.

Mr. Simon. And you say 125 lenders have joined the parent loan program compared to 384 lenders in the GSL.

Is that because it is more complicated or is it just simply because there has not been that much demand?

Mr. Cronin. We have a large number of very small banks. We have about 70 or 80 credit unions. Some of those have held off and one or two of the largest banks have held off until, as they put it, the Federal program stabilizes so that you don't have to reprogram the computer every few months.

There have been several banks expressing interest in when the Federal regulations are going to be finally approved. I believe for the entire 1981 year we were operating on the basis of draft or interim regulations. Some banks like the comfort of having final regulations in place before they embark on a new and potentially expensive program.

Mr. Simon. Mr. Hawk, I am intrigued by your reversal on the reinsurance idea.

Have you done any estimates at all, by any chance, of what impact that might have in dollar terms on Federal costs?

Mr. Hawk. Yes, sir. If you were to look at table 2 of my written testimony which appears on what would be page 13, following page 12 labeled as table 1, you will see a portrayal of the net savings per $1,000 in loans originated in the final left-hand column.

The first column shows the cost to the Federal Government at various default rates and I have listed a rate for default rather than total claims. You will note that I have added in, arbitrarily, 1 percent for death, disability and bankruptcy.

At a 5-percent default rate the net total savings per $1,000 of loans originated for the Federal Government is $12. And at a 10-percent default rate which would be an 11-percent claims rate including death, disability and bankruptcy, you will see the savings at $20 per $1,000 in loans originated.

The testimony says that you could reasonably expect savings in the amount of $18 per $1,000 in loans orignated over the life of those loans which would yield a savings of, based on $8 million in loans a year, $144 million on loans originated next year and each year thereafter.

So, Mr. Chairman, you have an opportunity to achieve a greater savings over the life of loans than what you are receiving presently with the origination fee without increasing the cost to the student while at the same time placing more responsibility and financial incentives on the guarantee agencies with respect to the defaults.

Mr. Simon. I am just curious, if I may ask the other two witnesses their reaction or have you heard of this report?

Mr. Cronin. Dick is always coming up with intriguing, sometimes radical proposals, Mr. Chairman.

We are assembling the 30 or 40 of the other State guarantee agencies on Thursday of this week to look at his proposals, to look at some of the proposals that Senator Schmitt and Senator Dominici are advancing and we will have a collective response and a position on cost-saving remedies coming out of our national council meeting on Thursday. I think we can probably get it to the committee within a week or 10 days.

All three of us will be there. It is going to take very careful study and review before we commit ourselves.

Mr. SIMON. Yes, I understand.

Ms. CROSS. One of the things that Dick did say was that he was speaking for his own agency and I think that that is important. The other aspect that is important is that the group is meeting Thursday to look at this proposal and other proposals and we admit that Dick is very persuasive.

One of the things I would like to comment on as it relates to the PLUS program, in New York we have similar concerns as it relates to getting banks involved in the program.

We currently have 169 out of approximately 400 lenders who have committed to the program. We see a situation where at this particular time the demand is not that high and as the demand increases, many of the other banks may be joining the program.

Our concern is that for this particular loan there may be limited access and that the assumption is that the cutbacks in the guaranteed student loan might be offset by the ALAS program and the PLUS program.

It is not our feeling that these cutbacks will be offset by these new higher cost loans, that for some students are just not available. Many of the banks perceive the PLUS program as a supplemental program, not as a program to take up the slack as far as the GSL program. And it may not be to the advantage of many parents or students to get involved in higher cost loans given their economic profile.

So we have some real concerns about unmet dollars because of the cutbacks in the programs.

Mr. SIMON. One final qustion, then I yield to my colleagues.

The Senate Budget Committee is working out, among other things, a proposal which would require of the students that they take a second loan for the interest on their loans.

In other words, it would increase student indebtedness appreciably.

I am just curious what your offhand reaction might be to the proposal. This is not a formal proposal of the Senate Budget Committee at this point but is being talked about over there.

Mr. HAWK. Well, Mr. Chairman, I would be happy to react in two or three different ways. Obviously, the thrust of that kind of a proposal is increasing the price substantially to the student, and reducing expenditures by the Federal Government.

The second component of my plan, of course, gets at the same cost area as does that particular proposal before the Senate Budget Committee.

The thing which I don't like about the proposal is that it tends to transfer the whole loan to the student and it seems to me that is entirely excessive.

The other thing I don't like is that it does not provide any opportunity for the student to gain the benefits as interest rates decline.

We run a risk during a period of high interest rates to load the student up as heavily as possible to save the Government from the high costs. Subsequently, if we have a decline in interest rates, which everyone keeps saying we are going to have, then the student, in fact, has a greater burden than is necessary.

I, personally, and I can't speak for my colleagues, would prefer to see a more modest shifting of the burden for the Federal Government and the students.

Mr. **CRONIN**. I took a look at this as one of 20 proposals that would save money and I wrote on the margin "kiting scheme." This is the way a number of countries finance their economy. I think Poland is one right now where they have to borrow large sums of money just to pay the interest on the money they have borrowed before.

This is one of the reasons for the deep crisis in that country right now.

Mr. Chairman, you and I remember that the city of Chicago just 2 years ago was rolling over and borrowing money to pay the interest payment on bad debts which facilitated a fiscal crisis and a new school finance authority similar to the other mechanisms that New York City had had to be put in place.

Families go out when they are in trouble, just before they go into bankruptcy court and have to borrow an additional loan to pay the interest on their other loans.

So if this is going to be part of consumer education for the next generation, that we encourage them at the beginning of their career to borrow money to pay the interest on other loans, we are going to have a very weird economy in the 21st century. I have some problems with it.

Mr. **HAWK**. Mr. Chairman, I might just add that the whole concept of borrowing interest to pay interest would put the students in the same kind of financial plight that many farmers in this country are in now when they have payments on loans due and they find themselves in a position to borrow funds to keep up the interest on loans to keep from going under.

Mr. **SIMON**. If I could just add, I am not advocating this by any stretch of the imagination but my fear is that as we look around for alternatives, as the pressure mounts in these coming weeks, all of a sudden some scheme like this is going to look attractive.

I hope it can be resisted and I hope the three of you and your counterparts will continue to monitor very, very closely what goes on in Washington in the coming weeks.

As the trial balloons go up I think many of them have to be shot down, probably most of them, if not all of them.

Mr. Peyser?

Mr. **PEYSER**. Thank you, Mr. Chairman.

I would first like to ask Mr. Cronin, dealing with the statements on the graduate student loan, as we know, the administration has now announced their plan, hopefully not the Congress plan but their plan—to terminate the graduate student from the guaranteed student loan program.

Do you have an estimate in mind as to what the impact would be if the simple change that was made as they have illustrated of simply making the graduate student now eligible for the parent loan as against the program that is now in place?

Do you have any graduate schools giving any indications as to what this might mean?

Mr. **CRONIN**. Yes, the preliminary reactions from graduate schools and there were some vivid quotes in the New York Times by at least one dean saying students, as soon as they heard it, have already begun thinking about dropping out of graduate school next year.

When the executive branch speaks, many people think, well, that is the way it is going to be next year. And it is going to have a very negative effect on graduate and professional school enrollments—a minimum of 10 percent, as many as 30 or 40 percent in certain schools.

I know I spent hours at Harvard University talking with all the aid officers. There will be schools like the business school, which has its own corporate sources—will be able to survive—and perhaps the law school. But the less financially endowed graduate schools, divinity, health, education, will suffer an immediate loss, apparently, as I said in the testimony, because we can't find banks that will make these ALAS loans.

If the student exercises the option, the yield to the bank is only this quarter a small percent.

It is a singularly unattractive credit mechanism for the banks and the students just will not be able to find the lenders. So it is a ticket to nowhere.

Mr. **Peyser**. Well, I appreciate hearing that because, certainly we are going to use that in an effort to counter what I would view as an absolutely outrageous proposal by the administration showing an absolute disregard for the very aims that the President said this country had to get on with when he took office, gaining in technological skills and in learning how to be more productive. He then proposes to eliminate graduate students, who presumably are among the most academically accomplished students in the country and make it impossible for them to go to graduate school.

I think there is a lot of misconception and I would welcome your thought on this.

I will use my own son, as an example, who is in graduate school presently. He has used the guaranteed student loan. He works 17 hours a week. He has just made loans through the school to get him enough money to finish out his year, and if he were faced with trying to pay interest payments each month, he would have been out of graduate school a year ago.

Now, do you have the feeling, based on your close work in this whole area, that graduate students, by and large, most are not either independently endowed or have parents who can afford graduate schol.

I have no objection to people who can pay their way. I think that is great. But for those who can't, is it your impression that most of them are trying to use all the devices they can, including working during school and making additional loans through school where available?

Mr. **Cronin**. Absolutely. Universities such as Tufts, Harvard, Boston University, a tremendous percentage of the students are working in the graduate schools; those that are married, the spouses are working to put them through and yet it is very difficult to make enough to meet the tuitions that are now six, seven, eight, up to $10,000 a year.

I mentioned medical, dental, and veterinary medical, which are well up into the teens.

The pressures are enormous and the accumulated debt tremendous. If you had to begin paying the interest in school you would either prolong the graduate program—it already takes too long for a Ph. D. Some of the master's programs that are part-time go 4 years. It is going to extend those even further.

One of the tragedies is that as we expand the defense budget, especially the contracts that are going to go to the northeast, a lot of them are going to generate an increased demand for electronics specialists, scientists, engineers, people in the computer area and the papers are already full of people who have a master's degree or more in terms of competence.

We will be closing the valves training just the people we need for the military system of the future. So it is going to work againat the national defense policy as well as national manpower policy to squeeze down the graduate students.

Mr. PEYSER. Thank you.

Mr. Hawk, perhaps I have not understood the proposal you have of saving the Government money by cutting back on the guarantee by the Federal Government.

As I listen to your statement, is the idea, as I understand it, that the student, the recipient of the guaranteed student loan would be the one whose interest rate would be adjusted as there was a change in interest rates and that they would have to repay that interest rate adjustment?

I am not quite sure I understand that. And do they pay it in the year that it is adjusted or is everything held off to the end of the line?

Mr. HAWK. Mr. Peyser, if I may, let's make sure that the two components to the plan as presented do not get confused.

The first component deals with the reinsurance arrangement and it is that component of the total plan which would transfer much of the burden for claims payments from the Federal Government to the guarantor without the heavy reimbursement which exists now.

Under that proposal the student would incur an increase in cost which would be essential for the guarantee agency to have the reserves necessary to assume that larger burden. But with the elimination of the origination fee the cost to the student remains the same, on the average, with little variation from one student to another.

But there is a savings to the Federal Government in a fairly significant amount. That is one thing by itself and I kind of like that.

I don't think that hurts students. I think it protects access. I think it places greater responsibilty and accountability on the guarantee agency.

The other component of the plan is designed to save or reduce Federal expenditures for the special allowance made to the lender. What that does is to say, "We will increase the rate on which, or at which the student makes repayments on a guaranteed student loan. We increase the interest rate from 9 pecent to 14 percent. Whether or not the actual cost to the student will be 14 percent or something less will depend upon what prevailing interest rates are during the life that that loan is outstanding. The cost but not the rate will fluctuate.

Mr. PEYSER. May I interrupt there just for a minute.

I was just doing some figuring here. If a student had started in your plan in 1968, he came under your loan plan in 1978, have you done any calculations as to what the cost to that student would be by the elimination of the special allowance?

Mr. Hawk. Mr. Peyser, I do not have that information immediately available.

Mr. Peyser. Generally, without getting into specific dollars, what do you think the increase impact would be? And would that be payable, that increase, would that be payable at the end of the loan just the way it works now or would that be payable during the period of the loan?

Mr. Hawk. Mr. Peyser, every quarter there would be a special allowance payment, a standard amount of 4 percent and there would be a formula which would determine what portion of that, depending upon prevailing interest rates in that quarter, would be allocated to principal reduction on the loan as opposed to simply interest supplement for the lender.

Now, the way the plan is presently written you would do those allocations once each year or at the time the loan is repaid just to save administrative costs.

Mr. Peyser. But the student does not pay anything during the interim period right now?

Mr. Hawk. Mr. Chairman, during the interim period of the loan the student would still not pay anything.

Mr. Peyser. That is what I want to be sure of. During that 4-year period, say the student is an undergraduate and these adjustments are going on are there no payments being made by the student?

Mr. Hawk. That is absolutely true.

Mr. Peyser. So at the end of the time an accumulated figure is then arrived at on the repayment, the increase. In other words, let's assume that the interest when he went in was 9 percent and when he came out it was 6 percent.

Mr. Hawk. Let me see if I can clarify. During the interim period of a loan while the student is in school, the amount of special allowance payment made by the Federal Government would be an amount which would vary below 4 percent because during the interim period of the loan there would be no payments by students.

The only thing paid by the Federal Government during the interim period of the loan would be the portion of the standard 4-percent special allowance which should be attributed to an interest supplement as opposed to interest reduction.

When the loan goes into repayment then the 4 percent would be allocated depending upon the rate.

The only change would be the student then would have no repayments during the interim period of the loan. The only change would be when the student went into repayment his repayments would be paid on a 14-percent interest rate instead of the 9 percent. Actual cost to the student would depend upon how interest rates fluctuated over the life of that loan.

Mr. Peyser. If the interest rate stayed over 14 percent he would certainly have 14 percent cost.

I would hope that the association and meeting would make a firm decision against such a plan because we fought like crazy in the conference when there was discussion with Senator Metzenbaum about the similar type of concept and the impact that would have on students making the loans to start with would be disasterous. We finally moved it up to 9 percent which was something I did not feel we should have done but nevertheless we did.

Basically what you are saying today, in spite of the President's hopes originally for a balanced budget in 1984 and interest back at 8 and 9 percent, the interest rates will be higher.

I noticed the banks have just increased the prime rate today going back to 16½ percent. The economists we met just a week or two ago tell us that they are now anticipating 17 and 17½ percent prime rates before the spring.

So, I would say that any move like this would have a disasterous effect on the student loan program and on students and I will certainly study it closer.

I am afraid I come into this with a very strong bias on what the implications of this would be. And so, while other members may not share that opinion at all with me, I think it is only fair you know where I would come down.

Mr. HAWK. Well, Mr. Peyser, I am glad to hear you say that. Perhaps I have not emphasized strongly enough my firm position that I don't think you should reduce costs for the guaranteed student loan program.

I am not here to advocate reduction of Federal expenditures for the guaranteed student loan program.

Mr. PEYSER. I am glad to hear you say that.

Mr. HAWK. If you look at the first three pages of my testimony you will see that it says you ought not reduce the cost but then it recognizes that you have a lot of pressures because of desires to increase costs for the military and that type of thing.

Mr. PEYSER. I hope that this Congress is no longer going to say that, well, we simply better start figuring out some alternatives because we are going to lose. That is why I am a little concerned to hear an alternate where a great deal of time is spent both in my discussion and your presentation that that is where we are going because I sure hope that that is not where we are going.

I have just a minute more time if I may and I just wanted to acknowledge to Dr. Cross, who is a representative of my State, that I am delighted that she is down here with us, that the survey that you are doing would be of utmost importance as the chairman indicated to us. Frankly, there are very few surveys that are out in this whole area anyway and certainly one that is as comprehensive as you are considering would be of great importance.

Now, the one question I would like to put to you deals again with your feeling at the graduate level, the impact in New York State and among New York State graduate schools that an elimination of a guaranteed student loan program would have.

Ms. CROSS. Congressman, as you may know, in the State budget, the colleges lost many lines and positions. There is great concern by the presidents in the private sector as well as the public sector about the cutbacks, namely as they relate to teaching and researchers that they need for colleges. There is a lot of concern.

We anticipate that 85,000 students will be affected by these changes.

I think the thing that is a big question for people in New York is what will be the cost of professional services should these students be forced to higher cost loans.

What will doctors charge in the future? What will researchers charge in the future?

What will various professionals charge in the future as a result of having to pay back these high-cost loans if this should go through?

So, given the cutbacks in the budgets that schools are experiencing and also the high dependency on graduate students as teaching and research assistants, it will be devastating to many of our colleges.

Mr. **Peyser**. I thank you very much, Mr. Chairman.

Mr. **Simon**. Mr. Erdahl?

Mr. **Erdahl**. Thank you, Mr. Chairman, and I apologize to you and to the panel for being tardy. We had another education subcommittee meeting on elementary and secondary education where similar concerns are being expressed.

Also, I am happy to see Mr. Hawk. He and I were together in the Minnesota State Capitol some years ago.

Maybe this was touched on before. One of the things that I have been mentally wrestling with because I don't view Dave Stockman as a social engineer, yet it seems as we look at some of the decisions that we are asked to make in this committee and in Congress and made in the first session of the 97th Congress, at a certain line that is hard to define, we cross over from making not only a financial budgetary decision but obviously some very fundamental social decisions.

We are saying, in effect, that if you, and your family, are at that economic level, you are going to be able to go to school or you are not going to be able to go to school, graduate school or college, with some few exceptions.

Obviously, some exceptional people move up and accomplish things but I think we are at a fundamental crossroad, determining, not only if a person goes to a school but what type of school.

You mentioned Harvard University where the tuition is rather high. Some other State-supported schools in New England, New York, and my State of Minnesota, have lower tuitions.

Maybe you would like to comment on that. Maybe that has already been discussed here today. What are we about as we are doing what we have been asked to do?

Mr. **Hawk**. Well, Mr. Chairman, if I may I would like to respond to that. Initially, very frankly, in the preparation of this testimony I wanted to come in and say you did two things that were bad last time.

Mr. **Erdahl**. We did more than two things that were bad.

Mr. **Hawk**. You increased the cost to the student with the origination fee which did not really serve any purpose. It was a budget line reduction.

The second thing which you did was you said, well, from now on we are not going to give the student, in many instances, the opportunity to assume responsibility for his or her own postsecondary education cost.

We are going to say the parents ought to pay that bill. We are going to establish a social policy which says a student ought not be responsible for his or her own postsecondary education expenses. That student's parents ought to be responsible for that.

And the decision we are really making is how much the Federal Government is going to pay and how much the parent is going to pay and not giving the student that opportunity.

I think that was a serious mistake. I decided politically not to come in and say what you did that time was not all that bad. You reduced Federal expenditures by restricting volume in the student loan program.

In order to restrict that volume you said we are going to require a family contribution which means the issue is not does the student need assistance in the first instance with respect to his or her own postsecondary education expenses but what portion is the parent going to pay and what portion is the Federal Government going to pay.

I think the implication of that is exactly what Mr. Erdahl is saying in making budget decisions. In this instance in restricting volume in order to meet a budget requirement you are, in fact, establishing significant social policy.

Mr. ERDAHL. Dr. Cross?

Ms. CROSS. One of the things that concerns me, as we look at the situation last year and the climate there was so little information about whether or not the savings could be achieved.

For example, when we get into discussions about the income cap, we know that States were never required to keep information on income for GSL so it got rather arbitrary. Should it be a $25,000 or $30,000 or $40,000 income cap?

I think the question that has to be raised and looked at is what information did we have to come to any kind of conclusions about what the savings would be. New information might suggest that you look at higher education as an industry, what happens to that industry.

As you look at loans as a self-help program, what happens to that whole concept of self-help?

But I think the larger question that we have to look at is, Is it cost effective to introduce these new loan programs which have to be marketed, which means adjustment in operations and adminsitraive details and which also may mean that both parent and students are put in an intolerable position,

For example, the point that Dick raised, the whole issue of parents having to be forced in some cases to take on a loan when they, themselves, may be at the point where they are planning to go back to school. So it is not only the imposition of a whole new philosophical position but it is also the whole question of whether or not it is cost effective and whether or not the so-called savings can be achieved.

Mr. ERDAHL. Thank you very much.

Dr. Cross, you made a point I would like to emphasize because it came up at a previous hearing. Mr. Peyser said maybe we should not knuckle under and say we will have to live with some cuts. Maybe we will be resisting some.

The point I want to repeat is the absolute necessity for distribution and dissemination of information to students and parents about what might be available in the area of student aid. We heard that maybe the breakdown in communication was at the high school level as far as assistance that might be available. This one underscored that.

But then also, Dr. Cross, you mentioned that in New York State there was a $275-million reduction that would be available for students from Federal assistance for post high school students. While we hear much about this new federalism, and the new volunteerism in the country, is somebody making this up to any significant degree, families, private sector, corporations, labor unions, State government? Where are these people going to go that have been looking forward to or depending on some assistance in the form of, I would guess, GSL or Pell grants, whatever it might be?

Ms. CROSS. At this particular time there is nothing on the drawing board to make it up. As you know, last year New York added $26 million to its tuition assistance program. With the cutbacks in the other programs I don't anticipate that the States will be able to make the cuts that have occurred in the Federal student financial aid programs.

I would like to mention, too, as it relates to information, we did do something which I consider very important. We disseminated to every high school student information on available student aid programs to help them figure out exactly what to do. But the information problem is the greatest problem which I feel parents are currently facing.

Mr. CRONIN. Congressman, if I could comment briefly. One is on the cost of education. I think most of us think that there is a great gap between Harvard and a few other colleges and the rest.

Actually, we are finding that the cost of going to a public university whether it is the University of Massachusetts or the University of Illinois where two of my children are attending, one is a sophomore right now and at the University of Minnesota the costs are up to $5,500, $6,000 a year if you are living on campus.

And we are finding out that the gap between Harvard and the other independent colleges and universities, the religious affiliated, Brandeis, Boston University, Boston College, they are just about $1,000, $1,500 behind some of the supposedly high cost or high tuition institutions.

So it is a problem that whether it is public or private the reduction and the availability of Pell grants and student loans and origination fees and the bites out of the apple that we are taking before giving it to the student are really working against meeting the cost of education.

I have got a longer paper which Tom Parker, a colleague, and I and one other have written, talking about the change in social philosophy away from a notion that was prevalent in the 1970's that the Government will help education and will help students have access.

Now, the shift in the last year or two has been toward saying, students, you help yourself and, by the way, we are going to make it costly for you but you invest in yourself.

And now we are saying, parents, you invest in yourself and we are on the verge of saying to graduate students, you invest in yourself and pay the interest simultaneously while you are going to school which is probably going to be the final straw that will break the back of graduate professional education.

But I will leave this paper which in somewhat more mellow terms describes the shift.

Mr. **Erdahl.** If I can just comment on that, Mr. Chairman, because we have three sons attending a fine private institution in Minnesota, St. Olaf College, and it is not that much less or more expensive than the other institutions. They are all expensive.

You have sons and Mr. Peyser has a son in graduate school and we have some in a private college. You and I may be in a higher salary category—ours as Congressmen is public knowledge—but there are a lot of people in this country that are trying to get by on half of that. I think here the determination comes that we are saying by these policies and programs that with very few exceptions families below a certain income level will not be able to send their sons and daughters to most colleges and universities.

I think what you said reinforces that and I did not think you meant it as a counter.

Mr. **Cronin.** That is right.

Mr. **Erdahl.** You described Richard Hawk as being a radical?

Mr. **Cronin.** Some of his most creative ideas are on the radical frontier. We expect that from Minnesota.

Mr. **Erdahl.** We expect that and we looked at him as being innovative.

Maybe you talked about it, I did not get a chance to read your statement yet. I think we are going to have to deal with limited funds, we have to acknowledge that. They are already limited.

The Washington Post tells us that further assaults are coming on many of these programs. What about the idea of different interest rates? Maybe as an incentive for paying back we could maintain the loans for college students at a low interest rate during the time a person is in college or graduate school, but following that to have a higher interest rate, maybe even the market rate or escalating up toward that as an incentive for repayment of the loans over a shorter period of time.

Are any of you people looking at that possibility as a compromise to try to make these funds available for some students that really need them if they are going to higher education?

Mr. **Hawk.** Well, Mr. Erdahl, with one little embellishment, that is really what the one component of the plan that I provided does. It causes the student to pay a higher interest rate and unless that interest cost fluctuated below 14 percent——

Mr. **Erdahl.** But when would that higher interest rate be kicked in, during the time of the repayment period?

Mr. **Hawk.** No, the Federal Government would continue to bear the cost while the student was in school just as the Federal Government does now.

It would affect the situation only during the period of repayment. That is, in effect, an increase in the interest rate to the student bringing it closer to market rate.

The only thing under that plan, his costs would never exceed 14 percent and his costs would fluctuate below 14 percent if the interest rates were lower than that.

Let me make it very clear. I am a little concerned that Mr. Peyser interpreted my presentation that I am here to advocate that some way or another we increase the cost to the student.

That could not be farther from the truth. All I am dealing with is the realities that this committee and the Congress is going to be under pressure once again to reduce Federal expenditure, I would like for you to look at an innovative, rather than radical plan, to permit you to do that in such a way which causes the maximum opportunity to the student to be preserved if those reductions are necessary.

Obviously, the first effort ought to be to resist any increases in the cost to the student.

I was very serious when I said that everything which this generation enjoys in terms of economic productivity, in terms of richness of life, in terms of sophistication of this civilization is due in large part because previous generations were making an ever-increasing investment in expanding educational opportunity.

That has been one of the hallmarks of growth we have seen in this society. We are never content to say, "Well, now, we have developed educational opportunities to this level. That is good enough and we will stop."

We have had an expansion of educational opportunity which has provided for continuous productivity and economic and social growth and that ought to be continued. You don't have opportunity unless you have economic access.

You have to have that economic access and it seems to me the guaranteed student loan program provides an excellent mechanism for doing that. You don't want the cost to be higher to the student than is essential.

All we are doing is recognizing the realities of the pressures which are going to be on this committee and we are saying, if you get in a situation where the program has to be cut, then please attempt to do it in some way which preserves the objective of the program and meets the student needs to the maximum extent feasible.

Mr. **Erdahl**. I appreciate the specificity of your explanation.

Dr. Cross?

Ms. **Cross**. I would like to comment that I think we would like to recognize the reality that the programs have already been cut; to look at some of the difficulties in perhaps instituting some of the new programs and to examine whether or not we should be looking at any alternatives at this present time.

What my presentation has suggested and what I would appeal for is a period of stabilization, some stability for students and parents and colleges and an examination of whether or not we have saved any money.

Is it best to save money at the cost of the industry of higher education and how should those savings be made.

I think that when we look at what reality we should be living with and accepting, we perhaps should be accepting the reality that we have already made certain cuts and that we don't know what these cuts have done. We should take a period of time to look at the fact that different sectors may be affected differently. There may be regional differences and these regional differences compounded with other differences in the regions could devastate portions of our population.

Mr. **Erdahl**. Thank you. What you say makes a lot of sense.

Thank you to members of the panel.

Thank you, Mr. Chairman.

Mr. **Simon**. We thank all three of you for your testimony. We will have some additional questions we had to submit for the record. You can respond to those.

Mr. **Cronin**. A point of personal privilege, Mr. Chairman, if the word "radical" could be struck from the record and the word "innovative" inserted.

Mr. **Simon**. Thank you very much.

[The information requested follows:]

Joseph M. Cronin
President

Berkeley Place at 330 Stuart Street
Boston, Massachusetts 02116

Telephone 617 426-9434

Massachusetts
Higher
Education
Assistance
Corporation

March 1, 1982

Mr. Bud Blakey
Ms. Maryln McAdam
U.S. House of Representatives
Subcommittee on Postsecondary Education
320 Cannon House Office Building
Washington, D.C. 20515

Dear Bud and Maryln,

The February Questions on PLUS/ALAS. Please tell the Committee:

1. Interest Rates
Borrowers would only borrow once per year. No problem. Banks change their prime rates, mortgage rates each month now, sometimes more often. It is normal.

2. Fluctuations
You could change the rates more often. I proposed June and December, just twice a year. Quarterly might be better.

3. Consequences
If PLUS interest rates stay at 14% for a full year and the prime rate drops, the T-Bill drops to 12 or 10%, then PLUS/ALAS will be an absolutely useless program, high and very dry on the shelf. As inflation drops, usually interest rates follow it down.

4. $3,000 A Semester
I really would prefer GSL to go to $3,000 a semester. Let my five kids borrow up to $6,000 a year! But this would mean a federal subsidy of up to 16% this quarter for each loan.

PLUS loans qualify for a 2% special allowance this quarter, one-eighth the cost of GSLs. Much less costly.

CBO can tell you more accurately than I how many schools have a cost of education above $6,000. Most are private colleges and serve less than 10% of the population. But they need the $6,000 option.

5. Paul Borden may present some cost-saving ideas. My task was to show you how PLUS can work better. The PLUGS and spouse loan idea will not cost. The twice a year rate adjustment will cost less than GSL changes. (See #4)

6. Verifications of income should be done by schools, not by lenders. The banks are not as good at this nor as willing. Many schools now ask for a 1040 form.

7. PLUS will grow rapidly because of last year's cuts in GSL eligibility and tuition increases at most colleges. ALAS will bomb.

If interest rates drop below 14%, PLUS will be a bomb, a source of ridicule, parents and grad students won't be able to get education loans, and the entire Cronin family will probably demonstrate in or near the Cannon House Office Building, third floor!

Sincerely,

Joe Cronin

Joseph M. Cronin
President

Thanks for asking!
Remember most banks prefer
variable rates on all the
new loans they make. A twice-a-year
revision is neither radical nor costly.
Joe

JMC/aml

HIGHER EDUCATION ASSISTANCE FOUNDATION

34 Corporate Woods, Suite 270
10950 Grandview
Overland Park, Kansas 66210
913-648-4255

March 31, 1982

The Honorable Paul Simon, Chairman
House of Representatives
Committee on Education and Labor
Subcommittee on Postsecondary Education
320 Cannon House Office Building
Washington, D.C. 20515

Dear Congressman Simon:

In accordance with your request, I am enclosing responses to the two sets of questions regarding my testimony before the Subcommittee on Postsecondary Education.

Because answers to several of the questions required a fairly extensive discussion of reinsurance, I have enclosed a paper titled, "An Analysis of Reinsurance and Federal Cost for Student Loans", to which reference is made in several of my responses. A review of this paper prior to reading the answers to questions may facilitate understanding of some of the answers.

Thanks to the Postal Service, your letter did not arrive until about thirty days following February 15. It was the late arrival of the letter and the complexity associated with some of the questions which has caused this submission to be so late.

Thank you for your continuing interest in preserving and strengthening the Guaranteed Student Loan Program. The courtesy and attentiveness of your Committee and its staff has been genuinely appreciated.

Sincerely,

Richard C. Hawk
Chairman of the Board

RCH/lb

Enclosures

AN ANALYSIS OF REINSURANCE AND FEDERAL COST FOR STUDENT LOANS

The data presented in the attached Tables I through IV demonstrate the effects of the current reinsurance arrangement on the distribution of the cost of defaults under the Guaranteed Student Loan Program between the federal government and guarantee agencies. All of the tables present the same information, but each table presents an analysis based on a different percentage of defaults, determined by relating the dollar volume of defaults over the life of all loans originated in a single year with the total dollar volume of loans originated in that year. Table I assumes defaults over the life of loans originated in each year equal 5% of the volume originated in the year, Table II assumes 10%. Table III assumes 15% and Table IV assumes 20%.

The tables show the annual "default rate" under the existing reinsurance arrangement (identified on the tables as "Net Claim Ratio") and the cost of reinsurance to the federal government per $100,000 in guaranteed loans originated each year (identified as "Federal Reinsurance"). Cost to the guarantee agency also is shown and is identified as "Net Claims Expense".

Because a purpose of the tables is to compare the annual "default rate" on which federal reinsurance is based under existing law with the actual percentage of loan volume which defaults over the life of a portfolio, all factors have been held constant for each year (for example, the volume of loans guaranteed is held at $100,000 in each year), and most factors have been simplified (for example, claims due to death, disability and bankruptcy are represented at .75% of loans originated and all of these claims are charged in the year following the loan in which each loan was originated).

Forecasts of loans entering repayment are based on actual experience of the Higher Education Loan Program of Kansas and assume that some loans begin repayment in the year following origination and that all loans are repaid fully by the end of the twelfth year. All default claims are charged during the year in which the loan enters repayment, and the relationship between default claim occurrence and loans entering repayment is a constant, true default rate.

Supporting detail for each of the tables is provided in Tables I.A. through IV.A.

Because the annual default rate based on the existing reinsurance methodology is affected by the original principal amount of loans which happen to be in repayment in the year prior to the year in which defaults occur, regardless of when loans in repayment were originated, actual experience will vary from the data presented in the table, due to changes in such factors as total annual volume and average loan size, which result in part from changes in program requirements from one year to the next. It is only by holding such factors constant that the impact of the existing reinsurance methodology can be demonstrated in a pure sense.

As demonstrated by the tables, the annual default rate under the existing reinsurance methodology is relatively high in the early years of a program and declines through about the eleventh year, at which point the annual rate reaches a relatively low level, which will remain constant for all subsequent years, so long as factors such as annual loan volume remain constant. A true default rate of 5% yields an annual default rate of .8% under the existing reinsurance methodology. Similarly, a true default rate of 20% ultimately yields an annual default rate of 3.6% under the existing reinsurance methodology. Because the federal government provides full reimbursement on claims paid by guarantee agencies each year until the annual default rate based on existing methodology exceeds 5%, the effect of the existing reinsurance methodology is to cause the federal government to bear the full financial burden of all default costs for a mature program in which factors such as annual loan volume remain constant, even if the true default rate is 20% or more.

This situation does not negate the need for guarantee agencies to establish and maintain substantial reserves to cover losses due to defaults because, even though the likelihood is that virtually all claims will be reimbursed by the federal government, anomalies in the pattern of annual loan volume and the rate at which loans enter repayment could expose the guarantee agency to substantial losses in a given year. Moreover, in the event of a complete disaster, it is unlikely that any guarantee agency would have sufficient reserves to meet its guarantee obligations, in spite of the fact that under normal conditions, the cost of all claims will be borne by the federal government. If, for example, all loans were to default in one year, the loss to the guarantee agency in a mature program would equal 18.6% of outstanding guaranteed loans.

With this background information on the effects of the present reinsurance methodology, comparison becomes possible with other approaches to federal reinsurance. One alternative approach was suggested in testimony to the House Subcommittee on Postsecondary Education by Richard C. Hawk on February 2, 1982.

The essence of that proposal is to relate claims to the original principal amount of loans originated in the year in which the non-repaid loan was originated, to treat reimbursement of all claims in the same manner (eliminate automatic 100% reimbursement to the guarantee agency for death, disability and bankruptcy), and to provide a reverse trigger mechanism on federal claims reimbursement, with no federal reimbursement until the claim rate reaches 5% and full reimbursement only of those claims occurring after the rate exceeds 12%. That proposal also included elimination of the administrative cost allowance which the federal government currently pays to guarantee agencies in an amount equal to 1% of loans originated each year.

Based on the model which generated the data for Tables I through IV, the effect of changing to the proposed reimbursement arrangement at both a 5% and a 20% true default rate for one year's loan volume in the amount of $100,000 is presented below.

	FIVE PERCENT TRUE DEFAULT RATE				TWENTY PERCENT TRUE DEFAULT RATE			
Portfolio Year	Current Federal Cost	Proposed Federal Cost	Annual Fed. Savings on Claims	Annual Savings on Claims Plus ACA	Current	Proposed	Savings	Savings Plus AC
1	$ 0	$ 0	$ 0	$1,000	$ 0	$ 0	$ 0	$1,000
2	1,649	0	1,649	1,649	4,340	0	4,340	4,340
3	1,604	0	1,604	1,604	6,410	4,775	1,635	1,635
4	1,251	0	1,251	1,251	5,000	4,875	125	125
5	1,251	601	650	650	5,000	5,000	0	0
6	0	0	0	0	0	0	0	0
7	0	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0	0
9	0	0	0	0	0	0	0	0
10	0	0	0	0	0	0	0	0
Total	$5,755	$ 601	$5,154	$6,154	$20,750	$14,650	$6,100	$7,100

Obviously, the effects become more pronounced with the addition of additional years of volume. Once again, using the model which generates $100,000 in loan volume each year, the effects of adoption of the proposed reinsurance arrangement are presented below.

ANNUAL SAVINGS
$100,000 CONSTANT ANNUAL LOAN VOLUME

YEAR	FIVE PERCENT TRUE DEFAULT RATE		TWENTY PERCENT TRUE DEFAULT RATE	
	Federal Savings From Claims	Savings on Claims Plus ACA	Federal Savings On Claims	Savings on Claims Plus ACA
1	$ 0	$1,000	$ 0	$1,000
2	1,649	2,649	4,340	5,340
3	3,253	4,253	5,975	6,975
4	4,504	5,504	6,100	7,100
5	5,154	6,154	6,100	7,100
6	5,154	6,154	6,100	7,100
7	5,154	6,154	6,100	7,100
8	5,154	6,154	6,100	7,100
9	5,154	6,154	6,100	7,100
10	5,154	6,154	6,100	7,100

If annual volume were $8 billion and the true default rate were 5%, the savings to the federal government in the first year after adoption of the proposed reinsurance arrangement would approximate $80 million, second year savings would exceed $210 million, and fifth year savings would be $490 million.

If the true default rate were 20% and the annual volume were $8 billion, savings to the federal government in the second year would exceed $425 million and fifth year savings would approach $570 million.

It should be noted that, as used in this context, savings to the federal government is achieved through a pure transfer of cost to guarantee agencies. In order to build adequate reserves to cover the increases in cost for claims, guarantee agencies obviously would have to charge guarantee fees well in excess of the currently authorized 1% per year for the interim period of the loan. As indicated in the testimony, a guarantee fee of 2-1/2% plus 2% per year for the interim period of the loan would be necessary, but with elimination of the 5% origination fee, average cost to the student would not increase.

On a cumulative basis, savings to the federal government over a twelve year period would exceed $5 billion based on a 5% true default rate, and $6 billion dollars based on a 20% true default rate. Cumulative savings per $100,000 of constant loan volume are presented below.

CUMULATIVE SAVINGS
$100,000 CONSTANT ANNUAL LOAN VOLUME

YEAR	FIVE PERCENT TRUE DEFAULT RATE		TWENTY PERCENT TRUE DEFAULT RATE	
	Federal Savings From Claims	Savings on Claims Plus ACA	Federal Savings on Claims	Savings on Claims Plus ACA
1	$ 0	$ 1,000	$ 0	$ 1,000
2	1,649	3,649	4,340	6,340
3	4,902	7,902	10,315	13,315
4	9,406	13,406	16,415	20,415
5	14,560	19,560	22,515	27,515
6	19,714	25,714	28,615	34,615
7	24,868	31,868	34,715	41,715
8	30,022	38,022	40,815	48,815
9	35,176	44,176	46,715	55,915
10	40,330	50,330	53,015	63,015
11	45,484	56,484	59,115	70,115
12	50,638	62,638	65,215	77,215

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TABLE 1

SUMMARY OF DEFAULT MODEL FOR HYPOTHETICAL PROGRAM 5% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	TOTAL
VOLUME/YEAR:	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	
CUMULATIVE SINCE INCEPTION:	100,000	200,000	300,000	400,000	500,000	600,000	700,000	800,000	900,000	1,000,000	1,100,000	1,200,000	1,300,000	1,400,000	1,500,000	
MATURED PAPER END OF PREVIOUS YEAR:	0	0	16,301	63,048	133,544	227,789	322,034	416,279	510,524	588,468	635,966	659,715	659,715	659,715	659,715	
DEATH, DISABILITY & BANKRUPTCY CLAIMS:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
DEFAULT CLAIMS:	0	898	2,502	3,753	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	62,197
TOTAL CLAIMS:	0	1,649	3,253	4,504	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	72,711
CLAIM RATIO:	100.0%	100.0%	20.0%	7.1%	4.3%	2.5%	1.8%	1.4%	1.1%	1.0%	0.9%	0.9%	0.9%	0.9%	0.9%	
NET CLAIM RATIO:	100.0%	100.0%	15.3%	6.0%	3.7%	2.2%	1.6%	1.2%	1.0%	0.9%	0.8%	0.8%	0.8%	0.8%	0.8%	
FEDERAL REINSURANCE:	0	1,469	2,981	4,444	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	5,755	72,199
NET CLAIMS EXPENSE:	0	180	272	60	0	0	0	0	0	0	0	0	0	0	0	[illegible]
FEDERAL REINSURANCE DETAIL																
DD&B @ 100%:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
5% @ 100%:	0	0	815	3,152	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	5,004	59,011
4% @ 90%:	0	0	587	541	0	0	0	0	0	0	0	0	0	0	0	[illegible]
BALANCE @ 80%:	0	718	828	0	0	0	0	0	0	0	0	0	0	0	0	[illegible]

TABLE II

SUMMARY OF DEFAULT MODEL FOR HYPOTHETICAL PROGRAM 10% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1969	1990	1991	1992	1993	1994	1995	1996	TOTAL
VOLUME/YEAR:	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	
CUMULATIVE SINCE INCEPTION:	100,000	200,000	300,000	400,000	500,000	600,000	700,000	800,000	900,000	1,000,000	1,100,000	1,200,000	1,300,000	1,400,000	1,500,000	
MATURED PAPER END OF PREVIOUS YEAR:	0	0	15,404	59,653	126,402	215,651	304,900	394,149	483,398	557,243	602,243	624,743	624,743	624,743	624,743	
DEATH, DISABILITY & BANKRUPTCY CLAIMS:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
DEFAULT CLAIMS:	0	1,795	5,000	7,500	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	124,295
TOTAL CLAIMS:	0	2,546	5,751	8,251	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	134,809
CLAIM RATIO:	100.0%	100.0%	37.3%	13.8%	8.5%	5.0%	3.9%	2.7%	2.2%	1.9%	1.8%	1.7%	1.7%	1.7%	1.7%	
NET CLAIM RATIO:	100.0%	100.0%	32.5%	12.6%	7.9%	4.6%	3.3%	2.5%	2.1%	1.8%	1.7%	1.6%	1.6%	1.6%	1.6%	
FEDERAL REINSURANCE:	0	2,187	4,967	7,587	10,383	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	10,751	132,634
NET CLAIMS EXPENSE:	0	359	784	664	368	0	0	0	0	0	0	0	0	0	0	2,175
FEDERAL REINSURANCE DETAIL																
DD&B @ 100%:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
5% @ 100%:	0	0	770	2,983	6,320	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	110,073
4% @ 90%:	0	0	555	2,148	3,312	0	0	0	0	0	0	0	0	0	0	6,015
BALANCE @ 80%:	0	1,436	2,891	1,705	0	0	0	0	0	0	0	0	0	0	0	6,032

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TABLE III

SUMMARY OF DEFAULT MODEL FOR HYPOTHETICAL PROGRAM 15% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	TOTAL
VOLUME/YEAR:	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	
CUMULATIVE SINCE INCEPTION:	100,000	200,000	300,000	400,000	500,000	600,000	700,000	800,000	900,000	1,000,000	1,100,000	1,200,000	1,300,000	1,400,000	1,500,000	
MATURED PAPER END OF PREVIOUS YEAR:	0	0	14,506	56,253	119,249	203,494	287,739	371,984	456,229	525,968	568,466	589,715	589,715	589,715	589,715	
DEATH, DISABILITY & BANKRUPTCY CLAIMS:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
DEFAULT CLAIMS:	0	2,693	7,502	11,253	15,004	15,004	15,004	15,004	15,004	15,004	15,004	15,004	15,004	15,004	15,004	186,492
TOTAL CLAIMS:	0	3,444	8,253	12,004	15,755	15,755	15,755	15,755	15,755	15,755	15,755	15,755	15,755	15,755	15,755	197,006
CLAIM RATIO:	100.0%	100.0%	56.9%	21.3%	13.2%	7.7%	5.5%	4.2%	3.5%	3.0%	2.8%	2.7%	2.7%	2.7%	2.7%	
NET CLAIM RATIO:	100.0%	100.0%	51.7%	20.0%	12.6%	7.4%	5.2%	4.0%	3.3%	2.9%	2.6%	2.5%	2.5%	2.5%	2.5%	
FEDERAL REINSURANCE:	0	2,905	6,955	10,541	14,424	15,272	15,693	15,755	15,755	15,755	15,755	15,755	15,755	15,755	15,755	191,830
NET CLAIMS EXPENSE:	0	539	1,298	1,463	1,331	483	62	0	0	0	0	0	0	0	0	5,176
FEDERAL REINSURANCE DETAIL																
DDAB @ 100%:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
5% @ 100%:	0	0	725	2,813	5,962	10,175	14,387	15,004	15,004	15,004	15,004	15,004	15,004	15,004	15,004	154,094
4% @ 90%:	0	0	522	2,025	4,293	4,346	555	0	0	0	0	0	0	0	0	11,741
BALANCE @ 80%:	0	2,154	4,957	4,952	3,418	0	0	0	0	0	0	0	0	0	0	15,481

TABLE IV

SUMMARY OF DEFAULT MODEL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	TOTAL
VOLUME/YEAR:	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	
CUMULATIVE SINCE INCEPTION:	100,000	200,000	300,000	400,000	500,000	600,000	700,000	800,000	900,000	1,000,000	1,100,000	1,200,000	1,300,000	1,400,000	1,500,000	
MATURED PAPER END OF PREVIOUS YEAR:	0	0	13,609	52,858	112,107	191,356	270,605	349,854	429,103	494,743	534,743	554,743	554,743	554,743	554,743	
DEATH, DISABILITY & BANKRUPTCY CLAIMS:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
DEFAULT CLAIMS:	0	3,590	10,000	15,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	248,590
TOTAL CLAIMS:	0	4,341	10,751	15,751	20,751	20,751	20,751	20,751	20,751	20,751	20,751	20,751	20,751	20,751	20,751	259,104
CLAIM RATIO:	100.0%	100.0%	79.0%	29.8%	18.5%	10.8%	7.7%	5.9%	4.8%	4.2%	3.9%	3.7%	3.7%	3.7%	3.7%	
NET CLAIM RATIO:	100.0%	100.0%	73.5%	28.4%	17.8%	10.5%	7.4%	5.7%	4.7%	4.0%	3.7%	3.6%	3.6%	3.6%	3.6%	
FEDERAL REINSURANCE:	0	3,623	8,942	13,491	18,321	19,430	20,104	20,500	20,751	20,751	20,751	20,751	20,751	20,751	20,751	249,663
NET CLAIMS EXPENSE:	0	718	1,809	2,260	2,430	1,321	647	251	0	0	0	0	0	0	0	9,436
FEDERAL REINSURANCE DETAIL																
DD&B @ 100%:	0	751	751	751	751	751	751	751	751	751	751	751	751	751	751	10,514
5% @ 100%:	0	0	680	2,643	5,605	9,568	13,530	17,493	20,000	20,000	20,000	20,000	20,000	20,000	20,000	189,519
4% @ 90%:	0	0	490	1,903	4,036	6,889	5,823	2,256	0	0	0	0	0	0	0	21,397
BALANCE @ 80%:	0	2,872	7,021	8,194	7,929	2,222	0	0	0	0	0	0	0	0	0	28,238

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TABLE I-A

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 5% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
PROGRAM YEAR 1982																
VOLUME	100,000															
DD&B		751														
DEFAULTS		898	1,604	1,251	1,251											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									16,301	30,446	23,749	23,749				
YEAR-END MATURED PAPER		16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749					
PROGRAM YEAR 1983																
VOLUME		100,000														
DD&B			751													
DEFAULTS			898	1,604	1,251	1,251										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										16,301	30,446	23,749	23,749			
YEAR-END MATURED PAPER			16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749				
PROGRAM YEAR 1984																
VOLUME			100,000													
DD&B				751												
DEFAULTS				898	1,604	1,251	1,251									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											16,301	30,446	23,749	23,749		
YEAR-END MATURED PAPER				16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749			
PROGRAM YEAR 1985																
VOLUME				100,000												
DD&B					751											
DEFAULTS					898	1,604	1,251	1,251								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												16,301	30,446	23,749	23,749	
YEAR-END MATURED PAPER					16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749		
PROGRAM YEAR 1986																
VOLUME					100,000											
DD&B						751										
DEFAULTS						898	1,604	1,251	1,251							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													16,301	30,446	23,749	23,749
YEAR-END MATURED PAPER						16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 5% DEFAULTS

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
PROGRAM YEAR 1987																
VOLUME	100,000															
DD&B		751														
DEFAULTS		898	1,604	1,251	1,251											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									16,301	30,446	23,749	23,749				
YEAR-END MATURED PAPER		16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749					
PROGRAM YEAR 1988																
VOLUME		100,000														
DD&B			751													
DEFAULTS			898	1,604	1,251	1,251										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										16,301	30,446	23,749	23,749			
YEAR-END MATURED PAPER			16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749				
PROGRAM YEAR 1989																
VOLUME			100,000													
DD&B				751												
DEFAULTS				898	1,604	1,251	1,251									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											16,301	30,446	23,749	23,749		
YEAR-END MATURED PAPER				16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749			
PROGRAM YEAR 1990																
VOLUME				100,000												
DD&B					751											
DEFAULTS					898	1,604	1,251	1,251								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												16,301	30,446	23,749	23,749	
YEAR-END MATURED PAPER					16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749		
PROGRAM YEAR 1991																
VOLUME					100,000											
DD&B						751										
DEFAULTS						898	1,604	1,251	1,251							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													16,301	30,446	23,749	23,749
YEAR-END MATURED PAPER						16,301	46,747	70,496	94,245	94,245	94,245	94.245	77,944	47,498	23,749	

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DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 5% DEFAULTS

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
PROGRAM YEAR 1992																
VOLUME	100,000															
DD&B		751														
DEFAULTS		898	1,604	1,251	1,251											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									16,301	30,446	23,749	23,749				
YEAR-END MATURED PAPER		16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749					
PROGRAM YEAR 1993																
VOLUME		100,000														
DD&B			751													
DEFAULTS			898	1,604	1,251	1,251										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										16,301	30,446	23,749	23,749			
YEAR-END MATURED PAPER			16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749				
PROGRAM YEAR 1994																
VOLUME			100,000													
DD&B				751												
DEFAULTS				898	1,604	1,251	1,251									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											16,301	30,446	23,749	23,749		
YEAR-END MATURED PAPER				16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749			
PROGRAM YEAR 1995																
VOLUME				100,000												
DD&B					751											
DEFAULTS					898	1,604	1,251	1,251								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												16,301	30,446	23,749	23,749	
YEAR-END MATURED PAPER					16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749		
PROGRAM YEAR 1996																
VOLUME					100,000											
DD&B						751										
DEFAULTS						898	1,604	1,251	1,251							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													16,301	30,446	23,749	23,749
YEAR-END MATURED PAPER						16,301	46,747	70,496	94,245	94,245	94,245	94,245	77,944	47,498	23,749	

TABLE II-A

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM   10% DEFAULTS

PAGE 1 OF 3

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
PROGRAM YEAR 1982																
VOLUME	100,000															
DD&B		751														
DEFAULTS		1,795	3,205	2,500	2,500											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									15,404	28,845	22,500	22,500				
YEAR-END MATURED PAPER		15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500					
PROGRAM YEAR 1983																
VOLUME		100,000														
DD&B			751													
DEFAULTS			1,795	3,205	2,500	2,500										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										15,404	28,845	22,500	22,500			
YEAR-END MATURED PAPER			15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500				
PROGRAM YEAR 1984																
VOLUME			100,000													
DD&B				751												
DEFAULTS				1,795	3,205	2,500	2,500									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											15,404	28,845	22,500	22,500		
YEAR-END MATURED PAPER				15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500			
PROGRAM YEAR 1985																
VOLUME				100,000												
DD&B					751											
DEFAULTS					1,795											
5 1,205 2,500 2,500																
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												15,404	28,845	22,500	22,500	
YEAR-END MATURED PAPER					15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500		
PROGRAM YEAR 1986																
VOLUME					100,000											
DD&B						751										
DEFAULTS						1,795	3,205	2,500	2,500							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													15,404	28,845	22,500	22,500
YEAR-END MATURED PAPER						15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500	

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DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 10% DEFAULTS

PAGE 2 OF 3

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
PROGRAM YEAR 1987																
VOLUME	100,000															
DD&B		751														
DEFAULTS		1,795	3,205	2,500	2,500											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									15,404	28,845	22,500	22,500				
YEAR-END MATURED PAPER		15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500					
PROGRAM YEAR 1988																
VOLUME		100,000														
DD&B			751													
DEFAULTS			1,795	3,205	2,500	2,500										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										15,404	28,845	22,500	22,500			
YEAR-END MATURED PAPER			15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500				
PROGRAM YEAR 1989																
VOLUME			100,000													
DD&B				751												
DEFAULTS				1,795	3,205	2,500	2,500									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											15,404	28,845	22,500	22,500		
YEAR-END MATURED PAPER				15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500			
PROGRAM YEAR 1990																
VOLUME				100,000												
DD&B					751											
DEFAULTS					1,795	3,205	2,500	2,500								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												15,404	28,845	22,500	22,500	
YEAR-END MATURED PAPER					15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500		
PROGRAM YEAR 1991																
VOLUME					100,000											
DD&B						751										
DEFAULTS						1,795	3,205	2,500	2,500							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													15,404	28,845	22,500	22,500
YEAR-END MATURED PAPER						15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 10% DEFAULTS

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
PROGRAM YEAR 1992																
VOLUME	100,000															
DD&B		751														
DEFAULTS		1,795	3,205	2,500	2,500											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									15,404	28,845	22,500	22,500				
YEAR-END MATURED PAPER		15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500					
PROGRAM YEAR 1993																
VOLUME		100,000														
DD&B			751													
DEFAULTS			1,795	3,205	2,500	2,500										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										15,404	28,845	22,500	22,500			
YEAR-END MATURED PAPER			15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500				
PROGRAM YEAR 1994																
VOLUME			100,000													
DD&B				751												
DEFAULTS				1,795	3,205	2,500	2,500									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											15,404	28,845	22,500	22,500		
YEAR-END MATURED PAPER				15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500			
PROGRAM YEAR 1995																
VOLUME				100,000												
DD&B					751											
DEFAULTS					1,795	3,205	2,500	2,500								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												15,404	28,845	22,500	22,500	
YEAR-END MATURED PAPER					15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500		
PROGRAM YEAR 1996																
VOLUME					100,000											
DD&B						751										
DEFAULTS						1,795	3,205	2,500	2,500							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													15,404	28,845	22,500	22,500
YEAR-END MATURED PAPER						15,404	44,249	66,749	89,249	89,249	89,249	89,249	73,845	45,000	22,500	

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TABLE III-A

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 15% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
PROGRAM YEAR 1982																
VOLUME	100,000															
DD&B		751														
DEFAULTS		2,693	4,809	3,751	3,751											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									14,506	27,241	21,249	21,249				
YEAR-END MATURED PAPER		14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249					
PROGRAM YEAR 1983																
VOLUME		100,000														
DD&B			751													
DEFAULTS			2,693	4,809	3,751	3,751										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										14,506	27,241	21,249	21,249			
YEAR-END MATURED PAPER			14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249				
PROGRAM YEAR 1984																
VOLUME			100,000													
DD&B				751												
DEFAULTS				2,693	4,809	3,751	3,751									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											14,506	27,241	21,249	21,249		
YEAR-END MATURED PAPER				14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249			
PROGRAM YEAR 1985																
VOLUME				100,000												
DD&B					751											
DEFAULTS					2,693	4,809	3,751	3,751								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												14,506	27,241	21,249	21,249	
YEAR-END MATURED PAPER					14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249		
PROGRAM YEAR 1986																
VOLUME					100,000											
DD&B						751										
DEFAULTS						2,693	4,809	3,751	3,751							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													14,506	27,241	21,249	21,249
YEAR-END MATURED PAPER						14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 15% DEFAULTS

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
PROGRAM YEAR 1987																
VOLUME	100,000															
DD&B		751														
DEFAULTS		2,693	4,809	3,751	3,751											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									14,506	27,241	21,249	21,249				
YEAR-END MATURED PAPER		14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249					
PROGRAM YEAR 1988																
VOLUME		100,000														
DD&B			751													
DEFAULTS			2,693	4,809	3,751	3,751										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										14,506	27,241	21,249	21,249			
YEAR-END MATURED PAPER			14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249				
PROGRAM YEAR 1989																
VOLUME			100,000													
DD&B				751												
DEFAULTS				2,693	4,809	3,751	3,751									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											14,506	27,241	21,249	21,249		
YEAR-END MATURED PAPER				14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249			
PROGRAM YEAR 1990																
VOLUME				100,000												
DD&B					751											
DEFAULTS					2,693	4,809	3,751	3,751								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												14,506	27,241	21,249	21,249	
YEAR-END MATURED PAPER					14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249		
PROGRAM YEAR 1991																
VOLUME					100,000											
DD&B						751										
DEFAULTS						2,693	4,809	3,751	3,751							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													14,506	27,241	21,249	21,249
YEAR-END MATURED PAPER						14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249	

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DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 15% DEFAULTS

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
PROGRAM YEAR 1992																
VOLUME	100,000															
DD&B		751														
DEFAULTS		2,693	4,809	3,751	3,751											
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000											
PAID IN FULL									14,506	27,241	21,249	21,249				
YEAR-END MATURED PAPER		14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249					
PROGRAM YEAR 1993																
VOLUME		100,000														
DD&B			751													
DEFAULTS			2,693	4,809	3,751	3,751										
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000										
PAID IN FULL										14,506	27,241	21,249	21,249			
YEAR-END MATURED PAPER			14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249				
PROGRAM YEAR 1994																
VOLUME			100,000													
DD&B				751												
DEFAULTS				2,693	4,809	3,751	3,751									
VOLUME TO REPAYMENT				17,950	32,050	25,000	25,000									
PAID IN FULL											14,506	27,241	21,249	21,249		
YEAR-END MATURED PAPER				14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249			
PROGRAM YEAR 1995																
VOLUME				100,000												
DD&B					751											
DEFAULTS					2,693	4,809	3,751	3,751								
VOLUME TO REPAYMENT					17,950	32,050	25,000	25,000								
PAID IN FULL												14,506	27,241	21,249	21,249	
YEAR-END MATURED PAPER					14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249		
PROGRAM YEAR 1996																
VOLUME					100,000											
DD&B						751										
DEFAULTS						2,693	4,809	3,751	3,751							
VOLUME TO REPAYMENT						17,950	32,050	25,000	25,000							
PAID IN FULL													14,506	27,241	21,249	21,249
YEAR-END MATURED PAPER						14,506	41,747	62,996	84,245	84,245	84,245	84,245	69,739	42,498	21,249	

TABLE IV-A

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
PROGRAM YEAR 1982													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1983													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

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DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
PROGRAM YEAR 1984													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1985													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
PROGRAM YEAR 1986													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1987													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32.050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
PROGRAM YEAR 1988													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1989													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
PROGRAM YEAR 1990													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1991													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
PROGRAM YEAR 1992													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1993													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
PROGRAM YEAR 1994													
VOLUME	100,000												
DD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		
PROGRAM YEAR 1995													
VOLUME		100,000											
DD&B			751										
DEFAULTS			3,590	6,410	5,000	5,000							
VOLUME TO REPAYMENT			17,950	32,050	25,000	25,000							
PAID IN FULL										13,609	25,640	20,000	20,000
YEAR-END MATURED PAPER			13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000	

Questions -- Richard Hawk Testimony

1. Q. As a priority you list low cost loans to students last. While that may be a reasonable priority from the perspective of the Guarantee Agencies, it isn't from the perspective of the U.S. Congress. The whole purpose of the GSL program is to provide low cost loans. I can agree that higher cost loans are preferable than no loan availability but I have difficulty ranking program simplicity and incentives for program operation above student need. Do you care to comment?

A. The reason for ranking "accountability and incentives for sound program operation higher than low cost to users of the program" is the belief that sacrificing accountability and sound operation as an expediency in order to keep the cost to the user low is self-defeating in terms of the long-range viability of the program. Practices which could lead to inordinately high default rates or failure of some guarantee agencies to be able to meet claims obligations could create the kind of crises leading not only to the collapse of the program but also to sufficiently negative attitudes toward loans to students that the very existence of loans as a mechanism for financing postsecondary education could be threatened. This clearly would not be in the long-range interest of students.

The ranking of "program simplicity" was viewed in a similar context. The difference is that the program ultimately could simply collapse under the weight of the additional complexity which seems to be introduced each time that the Congress acts to reduce program cost. It should be noted that the testimony states that, "this criterion must be applied with caution because simplicity just for the sake of simplicity is not nearly so important as meeting needs." The testimony concludes the discussion of this criterion with the statement that, "additional complexity might be preferable to more simple solutions which deny access to loans."

It should be noted that increasing the cost to the student is not desirable from the perspective of guarantee agencies. Cost increases to the borrower always impact the debt burden as compared with benefits to the student, increasing the potential for default and increasing risk to the guarantee agency.

The fact is that the Congress demonstrated a propensity last session both to reduce loan fund availability through imposition of the expected family contribution and to increase costs substantially by raising the interest rate from 7% to 9% and imposing a 5% origination fee. Given a demonstrated inclination to both reduce volume and also increase user costs, it seems appropriate to address attention to relative priorities, even though we oppose any reductions in the program. The effect of the priority rankings presented in the testimony is to say that, if the Congress deems that federal expenditures for loans must be curtailed, it is preferable to preserve short-term loan availability and long-term program viability than to destroy the usefulness of the program in meeting student needs by attempting to keep the price to the student low. In other words, it is better to have a viable program under which loans are available at some price than to have a program under which the price would be low if the student could find a loan, but probably cannot, or a program under which the long-term availability of loans is severely threatened, even though the price is low.

2. Q. Alternative I seems to have its greatest potential for the Guarantee Agencies if there is a high default rate. Many changes in the law and in the borrowing characteristics on the part of students indicate that a high default rate may become a reality. Do you feel that such characteristics as--
   *increased GSL borrowing by low income students to compensate for loss of monies from Pell Grants,
   *allowances for graduate and independent students under the auxiliary loan program, and
   *payment of interest while in school by students borrowing under the auxiliary program
   may lead to higher default rates?

   A. That guarantee agencies would fare better with adoption of the proposed change in reinsurance with a high default rate is questionable. As demonstrated in the enclosed paper, titled, "An Analysis of Reinsurance and Federal Cost for Student Loans," the current reinsurance arrangement is more favorable to guarantee agencies, even when 20% of loan volume goes into default. At 40%, guarantee agencies probably would be better off with the existing reinsurance arrangement, except that most guarantee agencies would not have sufficient reserves to manage the default rate, or to honor claims, at such a high level of defaults under the existing reinsurance formula, anyway.

   The relationship between borrowing by low income students and defaults is not direct, because repayment of student loans occurs after completion of the education when the student's income stream and potential for repayment reflect the advantage of the education. The field of study selected by a student has more to do with the student's capacity to repay a loan at the completion of the education than does the income of the student's parents at the time the education is pursued.

   Borrowing by graduate students and independent students under the auxiliary loan program clearly does have the potential to increase defaults because of the combination of increases in total debt and higher interest rates. Similarly, payment of interest by the borrower while in school increases the potential for default.

   The reality is that the program probably cannot survive if the default rate becomes high enough for guarantee agencies to fare better under the proposed reinsurance arrangement than the existing reinsurance arrangement.

3. Q. Doesn't the fact that a default rate of 12% or higher qualifies for 100% coverage from the federal government serve as disincentive for guarantee agencies to exercise diligence in maintaining low default rates?

A. Although the immediate economic incentive for guarantee agencies to maintain low default rates would disappear when the default rate exceeds 12%, the proposed reinsurance arrangement provides a much stronger incentive for the guarantee agency to attempt to keep the default rate under 12%. Moreover, guarantee agency personnel are perceptive enough to recognize that a default rate which continues to rise beyond 12% would threaten continued existence of the program. If survival of the program is not an adequate incentive for guarantee agencies to exercise diligence with respect to defaults, the amount of incentive provided under the existing reinsurance arrangement clearly is inadequate.

4. Q. Won't the elimination of the administrative cost allowance cause a hardship for newer guarantee agencies?

A. The administrative cost allowance would be less important for new guarantee agencies under the proposed reinsurance arrangement than it is now because the proposal would permit generation of adequate revenues to meet guarantee agency costs without the administrative cost allowance. The value of the administrative cost allowance is somewhat questionable for two reasons. First of all, the availability of the allowance is uncertain and cannot be depended upon but as a source of funds in constructing a guarantee agency budget. The administrative cost allowance is subject to the appropriations process and, even if funds are appropriated, payment of the allowance is at the discretion of the Administration. Second, the administrative cost allowance ultimately is paid so late that it is not useful for meeting cash flow needs within the year for which it is paid.

In spite of the limited usefulness of the administrative cost allowance, many guarantee agencies were established on the assumption that such a subsidy would be available and continuation of the administrative cost allowance for at least the first five years of each guarantee agency would be desirable.

5. Q. Would a variable academic cost allowance rate allowing higher payments to newer guarantee agencies be more equitable?

A. A variable administrative cost allowance, providing higher payments to newer, and lower payments to older guarantee agencies might very well be more equitable. In spite of an effort to conduct some analyses and to view this question from several perspectives, no definitive conclusion has been reached with respect to this question.

6. Q. Since the origination fee address a different problem than the restructuring of the reinsurance formula or the elimination of the administrative cost allowance is it not possible that a better alternative for the federal government would be to modify both rather than eliminate either one entirely?

A. Clearly, modifying both the origination fee and the administrative cost allowance could be accomplished in some combination. Indeed, a large number of possible combinations of actions with respect to the various program components could be developed in an effort to distribute expenditure reductions across the several components of the program.

7. Q. While you have stated that higher cost loans to students are better than no loan availability aren't you concerned that the high cost of loans will make them unattractive to students or will result in increasing defaults because of the inability of students to repay at the resulting increased rate?

A. Ideally, the Congress should seek to preserve both low cost to the student and general loan availability. As stated in the testimony to the Committee, "current and projected expenditures for the Program as presently structured represent a prudent investment in this nation's youth and the future contributions to the society and the economy from those who are assisted by the Program will multiply the return on this investment time and time again." The testimony also suggests that, "attention to reduction of expenditures would seem appropriate only in view of a compelling force which requires curtailment of both providing individual opportunities for the nation's youth and developing the nation's human resources."

If the Congress should decide that achievement of the ideal is not realistic and that there is a compelling force which requires that providing individual opportunity and developing the nation's human resources must be curtailed, then a lesser of evils must be selected. This, of course, is the context for the assertion that having loans available at some price is better than eliminating loan availability.

It is not intended to imply that increasing the cost of loans is desirable, and this is not intended to imply that no negative consequences are associated with increases in the cost.

There is a point at which the price to the student would be sufficiently high as to discourage utilization of loans in financing postsecondary education and to make the cost of the opportunity excessive. Given the factors that (1) the interest rate on student loans is presently well below market rates and (2) the increase in the interest rate to 9% did not appear to have an appreciable negative effect on the demand for loans, the current cost to the student seems to be below the cost level which would cause the cost to be more critical than availability, if that choice must be made.

Increases in the debt burden would have the potential for increasing defaults. On the other hand, making postsecondary education economically accessible is too important to eliminate loan availability because some borrowers will not be able to repay loans.

8. Q. In Alternative II you advocate increasing the interest rate on student loans to 14% and establishing a special allowance of 4%. How do you establish that 4% rate with fluctuating interest rates like we have seen in the last few years?

A. Alternative II was not presented to "advocate" increasing the interest rate on student loans to 14% and establishing a special allowance of 4%. Rather, the Alternative was presented to provide a mechanism for consideration if the Congress determines that the cost of the special allowance, which is the largest single cost of the GSLP, is greater than the federal government can afford. The way in which the 4% flat special allowance rate can be established with fluctuating interest rates is by increasing the rate at which the student pays interest to 14% and permitting the cost of interest to the student to fluctuate with market interest rates by causing a portion of the standard special allowance to be applied to principal reduction, rather than to interest, with the amount applied to principal reduction based on prevailing 91-day Treasury rate. The effect of the proposal would be to transfer the risk and associated cost of fluctuating rates from the federal government primarily to the borrower and partially to the lender.

9. Q. If interest rates rise above 18% or drop below 14% won't there be difficulties in finding lenders?

A. The 18% limitation on yield to the lender obviously would be a disincentive to the lender when prevailing interest rates exceed 18%. On the other hand, the lender would gain the benefit of an increase in the minimum return on a student loan from 9% to 14%. In addition, the proposal would increase the yield to the lender from T-Bill plus 3-1/2% to T-Bill plus 4%. The expectation is that the combination of the higher minimum and the increased yield spread would be sufficient compensating factors to make student loans an acceptable investment for lenders, even with the 18% ceiling.

10. Q. Is it possible that the amount of recomputation necessary to make the amortization of the borrower's principal amount when interest rates are either above 18% or below 14% might prove to be too costly for many lenders?

A. Every additional complexity in the program adds to the cost of the lender and serves as a disincentive for participation in the program. Accordingly, continuation of the present interest rate and special allowance arrangement is preferable to the change which is presented as a possible course of action, only if the Congress determines that the costs of the Program to the federal government as presently structured are beyond the capacity of the federal government.

11. Have you given any consideration to the effect 14% interest rates for students might have on default rates?

A. Any increase in cost to the student could lead to higher default rates. Similarly, a decrease in the interest rate could help in keeping default rates low. Unfortunately, estimating the increased cost to the federal government for defaults due to higher interest rates, and reductions in the cost to the federal government for defaults due to reductions in the interest rate is extremely difficult. Nonetheless, it seems reasonable to assume that reducing the interest rate would be advantageous both for stimulating loan utilization and for facilitating loan repayments.

12. Q. Alternative III assumes that the same students are served by Pell Grants and GSLs. This was never the intent of the Congress. Wouldn't this alternative alter the very nature of each of these programs and lack sensitivity to the needs of students in both?

A. Alternative III obviously is an extreme measure. Hopefully, circumstances are not so critical as to require measures so extreme. Clearly, grants which relieve the student of postsecondary education expense are more advantageous to the student than loans which simply permit the student to defer the expense of postsecondary education. Given the importance of education in a free society, a good case could be made for having the federal government bear a portion of the cost, perhaps the amount of tuition, for all students. The issue is not whether or not grants are desirable for the entire postsecondary education period. Rather, Alternative III is intended to address ways in which the federal investment in postsecondary education can be maximized if the Congress determines that support for students must be severely curtailed.

13. Q. What criterion would you use for eligibility under Alternative III -- current Pell Grant need analysis or the GSL needs analysis?

A. Although there clearly is some relationship between existing needs analysis systems and the relative difficulty which individual students and their parents may have in providing funds to meet educational costs, the needs analysis systems are probably more effective in causing a limited number of dollars to be distributed on a somewhat equitable basis or in limiting the amount of federal expenditures required in an entitlement program. Accordingly, the need analysis system selected for use probably would have to depend on the amount of funds which the federal government can provide in supporting students.

14. Q. It is understood that in many cases it is the parents of students who start making the initial repayments of loans until the student is adequately employed to assume the responsibility. Wouldn't forcing very low income students (those currently covered by Pell Grants) into borrowing under GSL result in increased default rates because these students cannot rely upon family resources for initial repayments?

A. If the intent of the Guaranteed Student Loan Program is to depend on parents for loan repayments in order to keep defaults low, the structure of the Program probably needs to be refined. Under the present structure, no attention ordinarily is given to either the capacity or the willingness of parents to participate in loan repayments. If the intent is to make loans available to students whose parents are willing and able to contribute to repayment, the parent probably should be required to co-sign the note and some assessment of the likely capacity of the parent to repay should be accomplished at the time of loan origination. The previous prohibition against collection of family financial information in the origination of loans presumably was intended to preclude the lender from discriminating among students according to family financial circumstances in originating loans. The current practice of collecting family financial information only when the adjusted gross income exceeds $30,000 per year, and the automatic eligibility for students below $30,000 per year, would seem inconsistent with any intent to preclude borrowing by lower income students or to depend on repayment by parents.

15. Q. How do you propose that very low income students could ever afford unsubsidized loans? Wouldn't your proposal lead students to go through 3 years of school but then find themselves unable to go the fourth year?

A. The proposed arrangement would have no direct negative impact on the ability of the student to meet postsecondary education costs in the fourth year, due to the arrangement for discounting interest and increasing the amount which the student is eligible to borrow. Accordingly, access to the fourth year would not be denied.

On the other hand, discounting of the interest for the fourth year would cause an increase in the amount of debt to be repaid after completion of postsecondary education.

16. Q. In testimony last week Dr. Edward Elmendorf, the Deputy Assistant Secretary for Student Financial Assistance stated that he felt the Department of Education had provided more than adequate funding to guarantee agencies to pay their operating costs, build resources and ... (question incomplete)

A. Although other guarantee agencies might disagree, the only federal subsidy absolutely necessary for guarantee agencies is the reinsurance. Although those guarantee agencies which did not receive federal reserve advances made available in 1965 may not be as comfortable as those which did receive the advances, those without, nonetheless, have been able to operate effectively. Although the administrative cost allowance has been useful in strengthening guarantee agency performance, availability of the administrative cost allowance is advantageous as an enhancement, rather than necessary as a condition for minimal viability of a guarantee agency.

SELECTED QUESTIONS CONCERNING GSL SAVINGS PROPOSALS OUTLINED IN TESTIMONY OF RICHARD HAWK, FEBRUARY 2, 1982

Reinsurance Proposal

1. Q. If the Federal Government were to assume 100 percent responsibility for State Guarantee Agency defaults when this default rate was 12 percent or more, what incentives would State Guarantee Agencies have to keep defaults low, especially if this rate was 12 percent or greater?

   A. In addition to the general concern over being recognized as a "high default" guarantee agency, and the fear of loss of the contract with the Secretary of Education for unsatisfactory performance, the economic incentive for the guarantee agency to keep defaults low under the proposed arrangement is that the guarantee agency would experience a financial loss for each default until the default rate exceeds 12%. Accordingly, so long as the default does not exceed 12%, any potential default averted yields a savings for the guarantee agency. Moreover, the proposed formula has the effect of an increased savings or economic reward to the guarantee agency as the default rate gets lower. Because the full cost of the first 5% of defaults would be borne entirely by the guarantee agency, the agency would have a strong incentive to keep the default rate well under 5%, if possible.

   Although it is true that the economic incentive to keep default rates low disappears when the rate on a portfolio exceeds 12%, the reality is that a 12% rate is sufficiently high to stimulate a strong desire on the part of guarantee agency personnel to demonstrate that every reasonable effort is being made to avert defaults. In the absence of economic conditions which generally preclude repayment of guaranteed student loans, a default rate which continues to rise beyond 12% would be sufficient to call into question the practices of the guarantee agency. Fear of reprisals for unsatisfactory performance ought to be adequate motivation for seeking to curtail defaults beyond the 12% rate.

   The advantage of the proposed reinsurance arrangement over the existing arrangement is that the economic incentive under the present arrangement becomes operative only after the default rate is relatively high. Under the proposed reinsurance arrangement the economic incentive is to perform effectively before the rate gets high.

2. Q. On page 7 of your testimony you suggest changing the determination of the "default rate" from "...the dollar amount of defaults/compared/ with the dollar amount of the original principal of all outstanding loans in repayment" to a relationship between "...claims paid to the original principal amount of loans originated in the year in which the non-repaid loan was originated..."
   a. Precisely what does this suggested change entail (perhaps a case study illustration contrasting the two methods would be helpful)?

A. Under the present reinsurance arrangement the default rate is influenced not only by the volume of loans which go into default in any year, but also by the volume of loans which happen to be already in repayment at that time. This is why 100% reinsurance for the first 5 years of operation of a guarantee agency is essential under the present reinsurance arrangement. Assuming an equal number of loans going into repayment each year, and assuming an equal percentage of defaults at the time loans go into repayment, the default rate under the present arrangement will be lower in the sixth year than in the first year. This is true, not because of any change in the rate at which loans default (the percentage has been held constant each year), but rather because the volume of loans in repayment has been increased simply by more years of operation.

The impact of the volume of loans in repayment on the default rate under the present reinsurance arrangement is demonstrated in the case study presented in Tables I through IV and the supporting detail for these tables in the enclosed "Analysis of Reinsurance and Federal Cost for Student Loans". These tables present the same information for a different percentage of loans originated in each year going into default over the life of those loans. The volume of loans originated has been held constant at $100 million for each year and the behavior of the portfolio with respect to such factors as when loans are converted to repayment and when defaults occur also has been held constant.

With 5% of the volume of loans originated each year going into default as presented in Table I, the annual default rate under the present formula, which is identified in the table as the Net Claim Ratio, declines from 2.2% in the sixth year of the program (1987), the first year for which the automatic 100% reimbursement would not be in effect, to .8% in the 11th year (1992), and will remain at .8% forever unless there is a change in either the proportion of loans originated which go into default or a change in the characteristics of a portfolio (volume, number of years in school, years in which defaults occur, etc.).

Under the 5% default model presented in Table I, the federal government bears the full cost of defaults because the annual rate calculated under the present reinsurance arrangement never exceeds 5% after the fifth year. Beginning with the fifth year, the annual cost to the federal government per $100 million of loan volume is $5,755,000.

In contrast, the annual cost to the federal government under the proposed reinsurance arrangement would be only $751,000 per $100 million of loan volume. Were it not for an assumed 3/4 of 1% rate of claims due to death, disability and bankruptcy, the cost to the federal government under the proposed formula at the 5% rate would, of course, be zero.

In summary, it is the combination of (1) calculating an annual default rate by comparing defaults in a year with loans in repayment in a year, and (2) the existing reinsurance formula which causes the lion's share of all claims costs to fall on the federal government.

b. What is the rationale for this suggested change?

A. The rationale for the suggested change is that the new arrangement would provide a clearer picture of the default situation because the default rate for each portfolio would not be affected by loans already in repayment from previous portfolios. Moreover, placing more of the financial burden for defaults on the guarantee agency (by, for example, having the agency bear the full cost of the first 5% of loans) would not be practical under the current reinsurance arrangement because, under the current arrangement, whoever is responsible for the first 5% of defaults in each year must bear virtually all default costs, even if $20 of every $100 in loans goes into default. The reserves required for lenders to accept the guarantee of guarantee agencies given that condition would be greater than feasible.

c. Would this suggested change generally result in a lower default rate than the present calculation?

A. The proposed change which would cause defaults to be viewed as a percentage of all loans originated in a year, would result in a substantially higher default rate than the rate derived by comparing loans which default in a year with loans in repayment in a year. This is vividly demonstrated by Table IV of the enclosed analysis, which shows the default rate over time calculated under the present formula, based on a constant $100 million per year with 20% of loans originated in each year defaulting during the life of each portfolio. Under the proposed method, the default rate for each portfolio would be 20%. As demonstrated by Table IV, the annual default rate (which is identified as the Net Claims Ratio in the table) under the existing method drops below 20% in the fifth year (1985), and continues to decline to 3.6% in the 12th year, at which it will remain forever unless there is some change in volume or loan portfolio characteristics.

Thus, it can be seen that, if the volume and other characteristics do not change, a default rate of 20% under the proposed method ultimately translates into an annual default rate of 3.6% under the current method.

d. Under what default assumptions would this suggested change save reinsurance costs for the Federal Government in the years ahead?

A. The suggested change would cause reinsurance savings for the federal government at all reasonably anticipated true default rates, even in excess of 20%, given constant annual volume. Based on the model utilized in enclosed analysis, cumulative savings to the federal government over the next 12 years would be $5 billion if defaults equaled 5% of loans originated and annual volume were a constant $8 billion. If defaults equaled 20% the savings over 12 years at $8 billion annual loan volume would be $6 billion.

3. Q. Assuming current GSL volume for the State of Kansas, what would be the comparable Federal and State Guarantee Agency unreimbursed outlays under the current and the proposed reinsurance programs, if the default rate were-- 5%, 10%, 15%, 20%?

A. Because the fiscal 1981 volume in Kansas was just over $100 million, the estimates provided in the enclosed paper, titled "An Analysis of Reinsurance and Federal Cost for Student Loans" provide a reasonable indication of federal and guarantee agency unreimbursed outlays under the two reinsurance arrangements, when multiplied by a factor of one-hundred.

4. Q. Under what circumstances would a State Guarantee Agency "make more" or "lose more" money under your reinsurance proposal when compared with the current reinsurance program?

A. It is difficult to conceive of a circumstance in which a guarantee agency would "make more" under the proposed reinsurance arrangement as compared with the existing arrangement over time. Because the existing formula is influenced so heavily by the number of loans which are in repayment in a year, it is possible that extreme fluctuations in annual volume could create a brief temporary situation in which a guarantee agency would "make more" under the proposed formula than under the existing formula.

As demonstrated by the data in the enclosed analysis, the guarantee agency clearly comes out better under the existing reinsurance formula with more than 20% of loan volume in default. The guarantee agency generally would fare better under the proposed arrangement only in the event of a complete disaster with respect to loan repayments, and this is as it should be. The purpose of federal reinsurance should be primarily to provide protection in the event of a disaster.

5. Q. What would be the effects of changing the existing reinsurance and reimbursement program--to modify the existing Federal reimbursement rate, or to continue the existing reinsarance program, but reduce the administrative cost allowance paid to guarantee agencies 4 or more years in existence to 1/2 percent? (Those established less than 4 years would continue at 1 percent.)

A. Preserving the present method of calculating the default rate for purposes of reimbursement, and changing the reimbursement rate to 100% through 3% of defaults, 90% from 3-8% of defaults and 80% from 9-100% of defaults would have relatively little effect on the federal cost for reinsurance so long as not more than 15% of loan volume goes into default. As demonstrated by Table IV in the enclosed analysis, the annual default rate (Net Claims Ratio) levels off at 3.6% when the true default rate is 20% and volume and other portfolio characteristics are held constant.

Reducing the administrative cost allowance paid to guarantee agencies four or more years in existence to 1/2" would, of course, achieve a savings equal to 1/2 of 1% of the annual volume originated by such guarantee agencies. This should not impair the program seriously.

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DEFAULT MODEL DETAIL FOR HYPOTHETICAL PROGRAM 20% DEFAULTS

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
PROGRAM YEAR 1996													
VOLUME	100,000												
OD&B		751											
DEFAULTS		3,590	6,410	5,000	5,000								
VOLUME TO REPAYMENT		17,950	32,050	25,000	25,000								
PAID IN FULL									13,609	25,640	20,000	20,000	
YEAR-END MATURED PAPER		13,609	39,249	59,249	79,249	79,249	79,249	79,249	65,640	40,000	20,000		

Special Allowance Proposal

6. Q. You propose to change the student loan interest rate from 9 percent to 14 percent and establish a fixed special allowance rate of 4 percent, with a variable share of this special allowance payment to be applied as an "additional payment" towards loan principal when market interest rates fluctuate between 14 percent and 18 percent. What consideration have you given to the possibility of higher defaults as college graduates face substantially higher repayment costs?

A. The proposed change providing a fixed special allowance of 4% would result in a higher average debt burden for students. Any change which increases the debt burden, whether a simple increase in interest or an increase in the amount which the student may borrow, has the potential of causing more defaults and, therefore, has some disadvantages. The change in the special allowance and corresponding interest cost to the student is presented as an approach to be considered only if it is determined that the cost of special allowance under the current special allowance formula is too great for the federal government.

7. Q. How will lenders be able to handle the complexities involved in applying payments to principal that will vary quarterly with changes in market interest rates, rather than using a fixed amortization schedule? --Won't such a system be too costly for many small lenders, thus driving them out of the GSL program?

A. The administrative complexities involved in applying payments to principal that will vary quarterly with changes in market interest rates will create problems for lenders, just as other complexities in the program create difficulties. It is in recognition of the additional administrative burden and the cap on the return to the lender that the proposal includes two revenue enhancements for the lender in addition to the benefit of a minimum 14% return. These measures to enhance the return to the lender are (1) a formula which increases the yield from T-Bill plus 3.5% to T-Bill plus 4%, and (2) requiring that principal reduction payments from the proposed special allowance be credited to the loan account only once each year, providing some float for the lender.

Under the proposal, the percentage of the special allowance payment to be applied to principal would be determined by the Department of Education, which would provide notification to the lender. The burden of actually crediting that amount to the loan account once each year would, of course, fall on the lender. The issue is not whether or not lenders can accommodate this additional administrative burden. Rather, the issue is whether or not the increased return to the lender is sufficient compensation to keep lenders involved in the program. Although most lenders probably would oppose this plan, most lenders also probably would decide that the compensation is sufficient for them to continue in the program, if the plan were adopted.

8. (No question was identified as Number 8 on the list of questions.)

9. Q. Could you elaborate on the "...additional administrative burden on the lender" mentioned in conjunction with this special allowance proposal on page 9 of your testimony?

A. The additional administrative burden on the lender is simply the activity of crediting a portion of special allowance payments to individual loan accounts as principal reduction pre-payments, and the associated accounting and clerical functions associated with that activity.

10. Q. What problems, if any, would you foresee in GSL lenders continuing to sell or warehouse student loans with Sallie Mae (or in other secondary markets) if the maximum student loan yield were limited to 18 percent, as under this proposal?

A. Limiting loan yield to 18% would cause SLMA to change its method of financing because it no longer would be able to borrow funds at a constant spread below the variable return on student loans. The result would be that SLMA would need to (1) either develop more complex and creative financing arrangements or (2) increase the price to the lender for sales. The limitation on yield as proposed should not have noticeable negative impact on state secondary market programs.

Other Savings Measures

11.Q. What is your reaction to the following additional suggestions for amending the GSL legislation to reduce Federal expenditures--
--by decreasing the special allowance percentage add-on (to the 91-day Treasury bill rate) from 3.5% to 3%?
--by placing an annual "ceiling" on GSL volume?
--by raising the "loan origination fee" from 5% to 10%?
--by establishing a GSL interest rate for students that accelerates according to a "fixed" schedule every couple of years while the loan is in repayment, with each percentage point increase in the borrower's interest rate matched by an equivalent percentage point decrease in the special allowance?

A. Decreasing the special allowance and reducing the return to commercial lenders from T-Bill plus 3.5% to T-Bill plus 3% would force commercial lenders to decide whether or not they will continue participation in the program at a reduced yield. Unfortunately, such a change would follow Congressional action last session which had the effect of reducing the yield to the lender by increasing lender cost as a percentage of funds in loans.

The expected family contribution provision has the effect of reducing loan size. Because costs remain constant for a loan account regardless of the size of the loan, a reduction in loan size increases the cost as a percentage of the dollar amount in loans. In the instance of a student seeking to borrow $2,000 with an expected family contribution of $1,000, the lender now must make two loans (one student loan and one parent loan) to meet a single $2,000 need, which previously the lender met with one loan. This, of course, doubles cost to the lender in meeting the $2,000 need.

In addition, because repayment on parent loans begins immediately, the lender experiences an increased cost in originating the loan, due to the necessity of collection and analysis of a different kind of financial information to determine credit capacity than was appropriate in the case of a student loan. Moreover, the lender does not have the benefit of the lower servicing cost interim period on the parent loan, so the effective return to the lender is depressed further by meeting part of the need through a parent loan. A decrease in the yield to the lender would seem less viable now than prior to the changes enacted by the Congress last session.

Although an annual ceiling on GSL volume is a simple means of limiting federal expenditures for the program, a ceiling has two very major disadvantages. First, unless the ceiling were set very high, it would have the effect of denying access to loans for some students. Second, because the postsecondary education population is mobile, because students begin at various times of the year, and because loans are originated by thousands of lenders, it is practically impossible to conceive of any workable means for adhering to the system while treating students and lenders somewhat equitably without having the entire system collapse under the weight of implementation complexities.

Raising the origination fee from 5% to 10% is a convenient mechanism for transferring cost from the federal government to the student. It also has the advantage of causing savings to the federal government to occur immediately. The long-term savings to the federal government would be substantially less than the long-term savings achieved through modification of the reinsurance arrangement, and the average cost to the student would be no greater than the cost to the student for an additional 5% origination fee.

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Mr. SIMON. Our next witness is Mr. Robert Turrill, vice president of the Howard Savings Bank of Newark, N.J.

We are pleased to have you here with us, Mr. Turrill.

STATEMENT OF ROBERT E. TURRILL, VICE PRESIDENT, HOWARD SAVINGS BANK, NEWARK, N.J.

Mr. TURRILL. Thank you.

The Howard Savings Bank is New Jersey's highest volume lender in the guaranteed student loan program, having provided more than $125 million in loans under that program.

We are also the State's highest volume lender in the more recent auxiliary loan program. In the first 4 months of the new program's existence in New Jersey, the Howard made 1,200 loans totaling almost $4 million.

Initially, we were almost as enthusiastic about the auxiliary loan program as we have been with the guaranteed student loan program.

It was a vehicle which allowed us to offer another valuable financial service to New Jersey residents, at yields and repayment terms satisfactory to the bank as an investment.

The program does provide for deferment of payment under various circumstances, which is a negative aspect from the view of the lender.

However, we reasoned that since the program directed itself to parents of students, the incidence of deferment would be minimal.

Our experience in the parent loan program has proven the accuracy of our prediction: of the first 990 loans made to parents, only two deferments have been requested.

Since October, when the program was expanded to permit loans to graduate and independent undergraduate students, our enthusiasm has diminished.

The problem, in our view, is that many of the borrowers will now be eligible for an immediate deferment and that deferment in many cases will run for several years.

While a loan is in deferment status the lender, at its option, may either capitalize the accrued interest or require the borrower to pay the interest periodically, such as quarterly or monthly.

The billing and collection of interest is burdensome to the lender, and the payment of that interest will be more of a burden on the borrower.

The monthly interest payment will be about 75 percent of the payment required when the borrower completes his studies and commences payment of interest and principal.

The capitalization of interest option, in its present form, is completely unacceptable to the lender because the anticipated 14 percent income from the borrower would be decreased substantially on those loans where the deferment exceeds 1 year. This is because the present language of the regulation prohibits the compounding of interest.

Interest calculations, when done to achieve a particular yield, presume annual compounding. Any deviation from that frequency will cause the effective yield to be either higher or lower than the anticipated yield.

In a 14-percent loan under this program, the capitalization of interest during a 2-year deferment would create an effective yield of 13.14 percent.

On a 3-year deferment the effective yield would drop to 12.40 percent; 4 years to 11.76 percent; and in a 5-year deferment the effective yield on this anticipated 14 percent investment would only be 11.20 percent.

In order to assure continued lender participation in this program, the option to capitalize interest must be made reasonable to us and this can be done by permitting interest compounding.

Ideally, the frequency of compounding should be quarterly, but no less often than semiannually. The slightly higher effective yield would be compensation for the absence of cash flow in this investment.

Obviously, this change would add nothing to the cost of the program. What may not be so obvious, is that the change would actually save taxpayer dollars because the Office of Education would be required to purchase fewer loans in default.

Those lenders who remain in the program under the present guidelines will not opt to capitalize interest, but will require the borrower to make interest payments during the period of deferment. Many of those borrowers will not have the wherewithal to service debt, and will default.

Finally, lenders need the assurance that these loans will be eligible for sale to the Student Loan Marketing Association, in order to create a form of liquidity for this otherwise long term investment.

Sallie Mae must be encouraged to complete the development of its purchase program, and I suspect that the prohibition of interest compounding will be a major concern of Sallie Mae's also.

Thank you.

[The prepared statement of Robert E. Turrill follows:]

PREPARED STATEMENT OF ROBERT E. TURRILL, VICE PRESIDENT, HOWARD SAVINGS BANK, NEWARK, N.J.

Mr. Chairman, members of the subcommittee, my name is Robert Turrill. I am Vice President of Howard Savings Bank, Newark, New Jersey. The Howard is New Jersey's highest volume lender in the Guaranteed Student Loan Program, having provided more than $125 million in loans under that program.

We are also the State's highest volume lender in the more recent Auxiliary Loan Program. In the first four months of the new program's existence in New Jersey, the Howard made 1,200 loans totaling almost $4 million.

Initially, we were almost as enthusiastic about the Auxiliary Loan Program as we have been with the Guaranteed Student Loan Program. It was a vehicle which allowed us to offer another valuable financial service to New Jersey residents, at yields and repayment terms satisfactory to the bank as an investment. The program does provide for deferment of payment under various circumstances, which is a negative aspect from the view of the lender. However, we reasoned that since the program directed itself to parents of students, the incidence of deferment would be minimal. Our experience in the parent loan program has proven the accuracy of our prediction: of the first 990 loans made to parents, only 2 deferments have been requested.

Since October 1, when the program was expanded to permit loans to graduate and independent undergraduate students, our enthusiasm has diminished. The problem, in our view, is that many of the borrowers, will now be eligible for an immediate deferment and that deferment in many cases will run for several years.

While a loan is in deferment status the lender, at its option, may either capitalize the accrued interest or require the borrower to pay the interest periodically, such as quarterly or monthly. The billing and collection of interest is burdensome to the lender, and the payment of that interest will be more of a burden on the borrower.

The monthly interest payment will be about 75 percent of the payment required when the borrower completes his studies and commences payment of interest and principal.

The capitalization of interest option, in its present form, is completely unacceptable to the lender because the anticipated 14 percent income from the borrower would be decreased substantially on those loans where the deferment exceeds one year. This is because the present language of the regulation prohibits the compounding of interest.

Interest calculations, when done to achieve a particular yield, presume annual compounding. Any deviation from that frequency will cause the effective yield to be either higher or lower than the anticipated yield. In a 14 percent loan under this program, the capitalization of interest during a two year deferment would create an effective yield of 13.14 percent. On a three year deferment the effective yield would drop to 12.40 percent; four years to 11.76 percent; and in a five year deferment the effective yield on this anticipated 14 percent investment would only be 11.20 percent.

In order to assure continued lender participation in this program, the option to capitalize interest must be made reasonable to us and this can be done by permitting interest compounding. Ideally, the frequency of compounding should be quarterly, but no less often than semi-annually. The slightly higher effective yield would be compensation for the absence of cash flow in this investment.

Obviously, this change would add nothing to the cost of the program. What may not be so obvious, is that the change would actually save taxpayer dollars because the Office of Education would be required to purchase fewer loans in default. Those lenders who remain in the program under the present guidelines will not opt to capitalize interest, but will require the borrower to make interest payments during the period of deferment. Many of those borrowers will not have the wherewithal to service debt, and will default.

Finally, lenders need the assurance that these loans will be eligible for sale to the Student Loan Marketing Association, in order to create a form of liquidity for this otherwise long term investment. Sallie Mae must be encouraged to complete the development of its purchase program, and I suspect that the prohibition of interest compounding will be a major concern of Sallie Mae's also.

Mr. SIMON. Thank you very much.

Maybe I should know, that but Sallie Mae does not now provide the paper?

Mr. TURRILL. That is right.

Mr. SIMON. And since October 1 when the program was expanded to permit loans to graduate and undergraduate students our enthusiasm has diminished, that is only to that portion of the program; is that correct? The parent program is still on line?

Mr. TURRILL. We are very happy with the parent program; yes, sir.

Mr. SIMON. Mr. Erdahl?

Mr. ERDAHL. Thank you, Mr. Chairman.

A question comes to mind that we have been talking about in several meetings, namely this whole area of default. The parent program is fairly new; but what about on the guaranteed student loans themselves?

What has the default experience been as far as people paying back the loans?

Mr. TURRILL. I am sorry I can't quote actual percentages to you but very acceptable to us, I almost don't want to say investment because there is no concern on our part since there is no risk in the event of a default from the standpoint of an investment.

However, there would be a concern if the key default rate was unusually high.

Mr. ERDAHL. You pay taxes like the rest of us.

Mr. TURRILL. We are speaking as a lender, not as a taxpayer. We would be concerned if the default rate was unusually high, then we would have additional servicing efforts on our part and we just don't want to have to service a lot of loans in default.

Mr. **Erdahl**. So that really has not been a serious problem because obviously you are aware of loans where there is default and the Federal Government participation?

Mr. **Turrill**. Oh, yes, the rate has been very acceptable.

Mr. **Erdahl**. Are you aware of what this might be in other institutions? I think the impression we get sometimes maybe comes from the media that all these students, to use the term of their generation, are ripping off the Government. Presumably people are not paying their loans back so we tried to get information on this at a previous meeting.

Mr. Peyser is not here now but he was pressing a witness on that point and it seemed to be that we would only find some isolated cases. Any one of them is too high because it does deprive some other student of access to these funds.

Mr. **Turrill**. The default rate in New Jersey has been very acceptable. I can say that at least for our State, speaking not only from the Howard standpoint but from the experience of other lenders.

We like the student loans. The guaranteed student loans, of course, are made with no examination on the part of the lender as to creditworthiness.

We are talking about the guaranteed student loan program at the moment because there is a lot more experience with that program.

Again, no determination as to creditworthiness. I would hate to make loans to parents of those people without the same kind of investigation as to creditworthiness.

Mr. **Erdahl**. Mr. Chairman. that brings about another question.

Do you have the latitude, with the loan to the parents to make this creditworthiness investigation?

Mr. **Turrill**. We do.

At the present time we are, in fact, drawing a file from the local credit bureau on parent loan applications. We are also allowed or permitted to design our own loan application form which we understand can include questions as to income and other debts being serviced at the present time.

We have not yet started to use our own revised form. We are still using the form provided to us by the guarantee agency which does not ask those questions.

So, to this date, we have not attempted to make any determination as to ability to pay since those questions are not asked on the application, questions as to income and present debts.

Mr. **Erdahl**. Mr. Turrill, do you see these loans for the parents as replacing or supplementing the guaranteed student loans?

Mr. **Turrill**. We see them as supplementing, sir.

Mr. **Erdahl**. Thank you very much. Thank you, Mr. Chairman.

Mr. **Simon**. If I could just toss one other question at you.

You are talking about the desirability of quarterly compounding.

Mr. **Turrill**. Yes, sir.

Mr. **Simon**. If you could have at least annual compounding, would these loans then become a more attractive reality?

Mr. **Turrill**. Certainly more attractive than they are today, sir. I am not sure that they would be enough to entice the lenders to remain in the program and capitalize the interest on those during the period of deferment.

Mr. **Simon**. One other question that is not central to this whole thing but I was interested in the testimony of Dr. Cronin that the parent loan, in fact, brought some customers to some of the banks making the parent loan.

Have you had any similar experience?

Mr. **Turrill**. Yes, sir.

Mr. **Simon**. Good. When you do good work it pays off once in a while.

We appreciate your testimony.

We would also like to submit some additional questions which you can answer for the record.

Mr. **Turrill**. Fine.

Mr. **Simon**. Thank you very much.

[The information requested follows:]

The Howard Savings Bank,
Newark, N.J., February 19, 1982.

Congressman Paul Simon,
Chairman, Subcommittee on Postsecondary Education,
Washington, D.C.

Dear Congressman Simon: Enclosed are my responses to the five questions included with your letter dated February 3.

If I may be of any additional assistance in your deliberations of the Auxiliary Loan Program, please be encouraged to call upon me.

Sincerely,

Robert E. Turrill,
Vice President.

Questions—Robert E. Turrill Testimony

1. We have received information from many lenders that they have reviewed the Auxiliary Loan program and found it unfeasible. Yet you state that Howard received the program enthusiastically. Why do you think your attitude and performance differs from that of other lending institutions?

Response: It probably would be more relevant, if I were able to respond to specific criticisms. However, as the Auxiliary Loan Program was first structured, that is, when eligibility was limited to parents of students, I am able to imagine only one valid reason lenders might have for lack of enthusiasm. Payment of the loans is guaranteed; the yield is adequate; the index provides assurance of future yield adequacy; costs of administration are no greater than those in conventional consumer loans, which assures reasonable net profit; and these loans offer an opportunity to establish additional banking relationships (through cross-selling) with new customers. In my mind, the only negativism toward the Parent Loan Program should be that until Student Loan Marketing Association develops a purchase program, these loans are long term, illiquid investments.

2. I am not sure I understand why you are having problems with compounding of interest for graduate and independent students. To my knowledge, the question of compounding is silent in the law. Why would you handle the interest for graduate and independent student loans differently from parent loans?

Response: Inherent in loans to parents is the fact that they seldom will be eligible for deferment, and they will be financially able to commence repayment immediately. It is not realistic to expect that repayment of loans to graduate and independent undergraduate students be handled the same as with loans to parents. While they are students, those borrowers are just not financially able to service debt to any degree, be it only accrued interest. Recognizing that they are not able to service debt, the most realistic approach would be to capitalize the accrued interest. This would forestall all repayment until the borrower is financially able, which would reduce the servicing efforts compared to billing and collecting interest on the part of the lenders. Of more consequence to the Federal Government is the fact that there should be fewer defaults in loans where no repayment is required until the borrower is financially able.

3. From what source have you received information that you cannot compound interest?

Response: Enclosed is a photo copy of page 30 of the guidelines for the Auxiliary Loan Program as provided us by New Jersey Higher Education Assistance Authority. After the definition of Capitalizing interest the following language reads, ". . . a lender may capitalize accrued interest covering any period in which the borrower is unable or is not required to make payments. The lender may add this accrued interest to the borrower's unpaid principal balance when the borrower is scheduled to begin or resume repayment." That last sentence clearly prohibits any compounding of interest.

Also enclosed is a photo copy of a letter to us from Richard Innocenzi, Director of NJHEAA, in which he states, in effect, that compounding is not allowed.

4. You state on page 2 of your testimony that interest computations "presume annual compounding", yet you advocate a change which will allow quarterly on semi-annual compounding. Wouldn't this serve to in fact result in greater profits to lending institutions while putting even greater burdens on the backs of the student?

Response: Yes, interest compounding done either quarterly or semi-annually would create an effective yield slightly higher than if compounding were done annually. Lenders need to be encouraged to capitalize interest during periods of deferment, but may be reluctant to do so due to the absence of cash flow, or payment of any kind. The slightly higher yield should be sufficient encouragement.

You are correct that this suggestion would put an additional burden on the borrower. Please remember that in your original request for testimony, you sought recommendations that would create better lender participation, but which would not add to the Federal Government's costs in the program. My recommendation would actually add slightly to the government's cost in that the quarterly special allowance would be based on increasing principal balances resulting from interest compounding. However the net result in cost to the Government would be lower, because if lenders are not encouraged to capitalize interest, those who remain in the program will elect to require payment of accrued interest during the period of deferment, which will result in a higher default rate.

5. You intimate that Sallie Mae will probably have difficulty with the interest compounding question. Do you have any specific and direct information from Sallie Mae that this is in fact the case?

Response: I have discussed the matter with Mr. Edward Fox, President of Sallie Mae. I believe that he agrees with my interpretation that interest compounding is prohibited. In my attempt to recall that conversation, I believe that I speculated that Sallie Mae would not be anxious to purchase loans wherein the effective yields would be subject to substantial reductions from "coupon" during periods of deferment. I received no denial from Mr. Fox as to that speculation.

State of New Jersey,
Department of Higher Education,
Trenton, N.J., December 23, 1981.

Ms. Darlene Walter,
Assistant Consumer Loan Officer,
The Howard Savings Bank,
Newark, N.J.

Dear Ms. Walter: Your interpretation of "capitalization" is correct. As you stated in your letter, it is the addition of accrued interest to the previously unpaid principal balance or tantamount to the compounding of interest.

If a lender chooses to capitalize on a PLUS or GSLP loan, it may do so, but not monthly, quarterly, or annually, but rather at the time the loan is converted to repayment. Hypothetically, if a graduate borrower under PLUS wishes to defer the interest, with the lender willing, for a period of two years, interest will be calculated at the end of 24 months, added to the original principal balance arriving at a new principal balance to be amortized over the number of months agreed. For purposes of billing, the federal government special allowance, the original principal must remain the same (if capitalized) or show a declining balance (if on repayment), but cannot increase.

I hope this answers the question posed in your recent letter.

Sincerely yours,

Richard J. Innocenzi,
Director, New Jersey Higher Education Assistance Authority.

Mr. **Simon**. Our final witness is Dr. Christine H. Rossell. Is she here?

[No response.]

Mr. **Simon**. If she is not here we have no further witnesses and our committee hearing stands adjourned.

[Whereupon, at 12:05 p.m., the subcommittee was adjourned.]

[The material submitted for inclusion in the record follows:]

OREGON STATE UNIVERSITY,
Corvallis, Oreg., February 4, 1982.

Representative JAMES WEAVER,
Washington, D.C.

DEAR REPRESENTATIVE WEAVER: Since Congress is holding hearings concerning the future of the federal Financial Aid program, I thought you might like to have the enclosed information about what is happening at Oregon State University and other schools within the State System of Higher Education in Oregon.

Sincerely,

ROBERT W. CHICK,
Vice President for Student Services.

[From the Daily Barometer, Feb. 4, 1982]

OSU RANKS AMONG BEST IN LOAN RETURNS

(By David Steinmetz)

Some students see school loans as virtual grants.

Others are careful to pay them off.

At OSU, apparently, most are careful to pay them off.

Dick Pahre, financial aid director, said the 4.49 percent default rate on National Direct Student Loans at OSU is "one of the lowest in the country." This default rate measures the percentage of loan dollars not paid by deadline, Pahre said.

This was the rate as of June 30, 1981.

Nationally, the rate was approximately 17 percent a few years ago, according to Tom Cooper, student loan fiscal officer. The highest default rate in the United States is 90 percent, at an Eastern university, Cooper said.

In a survey of seven Oregon schools, OSU was found to have the lowest rate, with the Oregon Institute of Technology holding the second-lowest default rate, at 7.59 percent as of June 30, 1981.

OSU's low default rate can be attributed both to students and to the OSU business office, Cooper and Pahre agreed.

"We have always concentrated on a low default rate," Cooper said. "We have always treated it as a loan."

Former students who are two weeks late in payment can expect a notice from the business office, Cooper said. After an additional week, a late fee is charged.

Two more weeks of delinquency brings another notice from the OSU business office.

If an additional two weeks pass and payment is not made, a personal letter is sent, he said. That letter is followed by a phone call if two more weeks elapse without payment.

Additionally, a fee is charged for late payment, Cooper said.

"We are willing to work with people," he added. "But if they don't cooperate, the account goes to a collection agency."

Cooper said accounts may be referred to the state revenue department or a private firm. At that time, the entire loan becomes payable, he said, adding that in extreme circumstances, accounts are pursued by a federal agency.

Rick Mattos, Southern Oregon State College business manager, said SOSC is among several Oregon schools that will be affiliated with OSU's computerized system, initiated to monitor loan payments and billing.

Other schools to be included in this system are Portland State University and Western Oregon State College, Mattos said.

According to Cooper, before federal authorities began pressuring universities a few years ago to collect federal loan repayments, some colleges and universities simply did not treat the NDSL as a loan.

"They (college and university officials) hadn't realized the importance of collection," Cooper said. "Maybe the administration hadn't placed enough priority on it, so (the loan office) was understaffed."

Cooper said that at some colleges and universities, a billing program for loan repayments had not even been established.

Schools are now required to pursue collection of loan payments in order to receive federal financial aid, Cooper said.

A proposed federal regulation, effective this spring, would cut off all federal loan funds to schools with default rates of greater than 25 percent and reduce federal loan funds for schools with rates between 10 and 25 percent.

Mattos said SOSC's default rate was 8.91 percent, as of June 30, 1981.

Other Oregon schools had the following default rates as of June 30, 1981: University of Oregon—7.94 percent, WOSC—10.62 percent, PSU—13.3 percent, Linn-Benton Community College—16.8 percent.

"I think that the students who attend Oregon State are responsible students," Pahre said, referring to the low default rate at OSU. "They are highly employable upon graduation, and are able to get good-paying jobs, and so are careful to pay it back.

"Students graduating in science and technical areas are more employable, also," he said.

Cooper agreed.

"Students at OSU are more technical and serious about school. Those type of people are more likely to get a high-paying job and be able to (repay their loans)," Cooper said.

He suggested that the low loan default rate at OIT may be because of its successful job placement record.

"We've always kept it (default rate) under 10 percent," said Jake Patterson, OIT business office manager, "due to a combination of a lot of things."

Among those "things" is the ability to remain in contact with students after graduation, a successful loan repayment collection system and a record of good job placement, Patterson said.

Payment on the NDSL must begin between six and nine months after leaving school, Pahre said, unless a deferrment can be made.

The interest rate on each NDSL is 5 percent and also begins six months after leaving school, he said.

OSU sets loan repayments to be completed within 10 years, hence a monthly payment on a $3,000 NDSL would be approximately $30, Cooper said. But he added that payments vary according to the size of the original loan.

OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

WEDNESDAY, FEBRUARY 3, 1982

House of Representatives,
Subcommittee on Postsecondary Education,
Committee on Education and Labor,
Washington, D.C.

The subcommittee met, pursuant to call, at 10 a.m., in room 2261, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Peyser, Weiss, and Erdahl.

Staff present: William A. Blakey, counsel.

Mr. Simon. The Subcommittee on Postsecondary Education today continues its oversight hearings on the major Federal student assistance programs. We will hear from representatives of the General Accounting Office regarding their recent reports on satisfactory academic progress, the effectiveness of institutional repayment and collection practices in the national direct student loan [NDSL] program, and the Department of Education's management of the guaranteed student loan [GSL] program.

We will also hear from two college presidents who are building a successful record of collecting NDSL loans. I hope their testimony can provide some useful advice to others who may be adversely affected by the Department's new "due diligence" regulations. Reverend Weiss, I understand, will be commenting on these regulations.

This brings me to my final point. While I favor doing everything we can to improve institutional collection efforts, I am concerned that we not penalize the current generation of college students—or the next generation—because an institution is not making a satisfactory effort to collect overdue or defaulted NDSL loans.

When capital contributions are reduced, students are denied loans. The school suffers, but only indirectly. Students pay a high price for lack of institutional effort and for the sins of their predecessors.

Let me just add one final point. As far as the chairman is concerned, and I think I speak for the majority on this subcommittee, what we are interested in is the effective implementation of these programs.

We are not interested in cutting them off. If institutions should be punished in some way, the students who need the loans should not be punished in the process.

I am very pleased to have as our witnesses Gregory J. Ahart, the Director of the Human Resources Division of the General Accounting Office, accompanied by Alfred P. Shane, Alfred R. Schnupp, and Frankie Fulton.

I am pleased to have you here and you may proceed.

STATEMENT OF GREGORY J. AHART, DIRECTOR, HUMAN RESOURCES DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY ALFRED P. SHANE, ALFRED R. SCHNUPP, AND FRANKIE FULTON

Mr. **Ahart**. Thank you, Mr. Chairman, I would, with your permission, like to file my full statement for the record.

We are pleased to be here this morning to discuss three reports of GAO concerning the academic progress standards for students receiving Federal financial aid; the collection of defaulted national direct student loans and the guaranteed student loan information system.

Our report on the need for tougher academic progress standards, which was dated December 3, 1981, concerns programs administered by the Department of Education, of the Veterans Administration, and the social security Administration. These programs provided about $6.8 billion of aid during fiscal year 1980 to students.

We reviewed the transcripts and financial aid records of almost 6,000 students randomly selected out of a universe of 49,250 aid recipients at 20 schools in 12 States. The schools represent a broad cross-section of higher education, considering type, support, educational purpose, and location.

An effective academic progress standard should accurately measure both the quality of the student's work and the rate of progress toward a definite educational goal, and include reasonable and consistent requirements for such factors as grade point average, nonpunitive grades which do not affect the GPA or count toward program completion, the rate of movement toward completion of a course of study, and related elements.

In our opinion, an academic progress standard which does not consider these factors does not adequately measure progress, even though it may be in technical compliance with Federal regulations.

VA, which provides education and training benefits to veterans and eligible dependents, requires each participating institution to have VA-approved standards of progress and to enforce certain requirements set by law and regulation.

The Department of Education, which provides aid under several programs, leaves the determination of academic progress largely to the institutions themselves.

SSA, which provides benefits to children of deceased, retired, or disabled social security contributors, has established no academic progress standard since the Social Security Act requires only that eligible students attend school full time.

The standards in effect at the schools we visited were often not adequate. Many students' grades were low and often inflated by the overuse of nonpunitive grades. Progress toward educational goals was often slow and, in some cases, virtually impossible to determine.

Institutions generally use the grade point average as a key indicator of academic quality. To graduate, a student would normally have to attain a C average, or a grade point average of 2.0 on a 4.0 scale, but institutions frequently allow students to maintain grade point averages below 2.0, particularly during the first few terms.

Many students receiving aid at the schools we visited had cumulative grade point averages well below graduation requirements. For example, almost 20 percent of the Pell grant recipients and 23.1 percent of the SSA recipients had cumulative averages below 2.0. About 9.5 percent and 10.8 percent, respectively, had averages below 1.5, the equivalent of a D-plus. Fewer VA students had low averages, with 12.4 percent having grade point averages below 2.0 and 3.5 percent below 1.5.

The concept of satisfactory academic progress include quantitative as well as qualitative standards. That is, the student should be moving toward an educational goal at a reasonable rate.

The agencies included in our review did not specifically require such quantitative measures and only 10 of the 20 schools visited had them. The absence of such standards can lead to students remaining in school with financial aid for a long time, particularly under the Pell grant program where there is no limit on the number of school terms for which financial aid can be provided.

For example, one student had been enrolled for 5 years, receiving more than $4,200 in Pell grants, but was academically a second-quarter sophomore. Some students had been in school up to eight academic years.

There is no benefit to setting either qualitative or quantitative standards if an institution does not enforce them. We found, however, that 9 of the 20 institutions we visited were not fully enforcing their published standards.

At the nine schools, we estimated overpayments of about $1.3 million to recipients of Department of Education aid. We did not project overpayments for VA.

A student at a private 4-year college, for example, received $15,587 in Department of Education aid over a 5-year period, earning 65 semester hours with a 1.35 grade point average. Had the aid been terminated after 2 years, as required by the school's standard, $9,136 in aid could have been saved.

We believe a uniform Federal policy for academic progress standards is needed. Although standards set by existing VA legislation and regulations are generally adequate, VA does need standards for the rate at which a student is progressing.

Additional requirements are especially important for the Department of Education, since the Pell grant is available to a qualifying student for as long as it takes to get a degree.

We believe that changes to the authorizing legislation and program regulations to strengthen academic progress requirements would result in savings in Federal funds now being paid to students who are not making satisfactory progress; fewer differences in Federal requirements encountered by institutions in establishing standards for students under the three programs, and better coordination of Federal efforts to establish and monitor enforcement of academic progress requirements.

In our report, we recommended that the Congress enact legislation to require satisfactory academic progress for SSA student aid recipients, and to authorize the Departments of Health and Human Services and Education to issue regulations setting forth general standards for institutions to follow in establishing such academic progress standards.

We recommended also that, in issuing regulations on academic progress, the Secretaries of HHS and Education consider a number of factors similar to those now in effect for VA students.

We recommended that the Administrator of VA require institutions to include quantitative measurements for academic progress.

Finally, we recommended that the Director of OMB ensure coordination by the other three agencies in setting and enforcing requirements on academic progress.

OMB generally agreed with our recommendations. HHS did also, but questioned the usefulness of implementing standards for its program, which is being phased out. VA did not agree with our recommendation, claiming it would be unworkable and an administrative burden. Education has not commented on our recommendations.

But I understand they did inform the subcommittee last week that they are in general agreement with and are moving to pursuing regulations.

Turning now to our report for the need of stronger actions to recover defaulted national direct student loans, dated September 30, 1981, since this program began in 1958, nearly $5 billion in Federal funds have supported loans to about 11 million students.

The program has been plagued by high default rates. The default rate as of June 30, 1980 was 16.3 percent, with outstanding defaulted loan balances in excess of $830 million. Nearly 1,200 schools had default rates of 20 percent or higher; 315 schools had default rates exceeding 41 percent.

Our review focused on determining how well schools are carrying out their responsibilities for administering and collecting student loans and identifying Department of Education actions for collecting defaulted loans forwarded to it by participating schools.

We visited seven schools in the Midwest with default rates ranging from 5.9 to 63.1 percent and obtained information on about 600 defaulted loans. Six of these schools had default rates exceeding 20 percent. The seven schools were judgmentally sampled; therefore, the observations on loan collection procedures relate only to these schools.

We also obtained information on defaults and collections for 33 other schools in the same geographical area, that is the Midwest, with default rates exceeding 20 percent.

Schools are responsible for making loans and collecting repayments either themselves or through agents. Department regulations require schools to be diligent and forceful in administering and collecting student loans.

The seven schools we visited did not fully comply with Education's loan collection procedures. Though they generally did an adequate job sending bills and collection letters, improvements were needed in other areas. For example:

Some schools were remiss in counseling borrowers and maintaining contact with them.

Most of the schools had problems locating borrowers with whom they had lost contact.

Schools often did not refer accounts quickly to collection agencies, monitor the status of accounts referred, and determine the collection agencies' success.

The seven schools had been reluctant to sue borrowers to collect defaulted loans.

Several school officials believed that referring names of defaulted borrowers to credit bureaus could aid in collecting defaulted loans by providing an incentive for repayment, but under the Family Rights and Privacy Act according to Education, there were only limited situations in which a credit bureau would be authorized to disclose information about a defaulted loan to a third party.

Education has since obtained a legal reinterpretation of the act. Credit bureaus can now enter student loan information into the credit information mainstream as they would any other credit information.

Schools are permitted to forward loans to Department of Education for collection. As of September 15, 1979, Education had received about 240,000 defaulted loans with outstanding loan balances of nearly $215 million. Through March 1981, it had collected $5.8 million, most since December 1980.

Many of the loans turned over to Education by schools we visited were in default for a number of years, which could make collection difficult. By law, loans must be in default for at least 2 years before they can be turned over. School officials and Department regional office collection officials believed that forwarding defaulted loans to Education sooner could help to increase collections.

Education plans to reduce the number of its collectors from 955 to 250 by early 1982, and to contract out collections of defaulted loans. I understand they discussed this with the subcommittee last week.

A Department task force study and a contracted study concluded that use of private collection agencies would be at least as cost-effective as the use of departmental collectors.

However, the statistics contained in these studies do not conclusively support that contention. The contracted study's cost data indicated that the collection efforts in one Education region were clearly outstanding and could not be duplicated by a private contractor.

To strengthen collection activities of the program, we recommended that the Secretary require schools to comply with the Department's loan collection procedures, particularly with respect to bringing suit against defaulted borrowers and submitting defaulted loans more quickly to collection agencies; require schools to monitor results of collection agencies' actions; establish an acceptable default rate and suspend from the program or withhold Federal funds from schools that exceed the established default rate; determine whether submissions of national direct student loans to Education for collection earlier than the statutory 2-year time limit would be beneficial to collection efforts, and if so, consider proposing legislation to allow schools to submit defaulted loans as soon as possible after completion of required collection activities; advise schools and credit bureaus of Education's reinterpretation of the law that credit bureaus can redisclose student default data, and, finally, monitor the Department's use of private collection agencies to insure that their use is the most cost-effective means of collecting defaulted student loans; any reassessment should consider the collection program that was in place in Education's San Francisco region that was returning approximately $6 for every $1 spent.

The Department, in this case, agreed with most of our recommendations.

Finally, I would like to turn to our report on the guaranteed student loan information system, which is dated September 24, 1981. This report was requested by the Subcommittee on Intergovernmental Relations and Human Resources, House Committee on Government Operations, which was concerned over the lack of progress in developing and operating an adequate automated information system for processing transactions, maintaining financial accounts and producing reports to operate and manage the Guaranteed Student Loan program.

This program guarantees loans from eligible lending institutions to undergraduate and graduate college student in two ways: Insuring the loans directly by the Federal Government, or reinsuring loans insured by States—State agency loans.

In fiscal year 1980, the program, one, insured $504 million in Federal loans and reinsured $4.3 million in State agency loans; two, paid about $130 million for defaulted Federal loans and $157 million for defaulted State agency loans; three, recovered about $40 million and $25 million in student loan default collections from the Federal and State programs, respectively, and, four, paid interest and "special allowances" totaling about $1.1 billion to lenders for both types of loans.

To keep track of and control this multibillion-dollar program, the office maintains a computerized information system to process most program transactions. This information system has been plagued with problems for years, and millions have been spent trying to resolve them.

A major focus of our review was to determine the efforts and plans to correct known deficiencies in the system.

To meet this objective we reviewed program activities at program office headquarters in Washington, D.C., and at the three largest regional offices, San Francisco, Chicago, and Atlanta, to learn how well the system was meeting the program's needs, and interviewed a cross section of information system managers and users concerning what the program office had done and planned to do about correcting these deficiencies.

We also contacted State guaranty agencies in Virginia, Pennsylvania, and New Jersey and obtained 52 student loan histories from the States to check for instances of reinsurance transactions that conflicted with Federal regulations.

We concluded that the system continued to be deficient in the following four major areas:

First, State agency loans were automatically reinsured regardless of whether the student was qualified under the law and regulations. We determined that some loans to students who had exceeded loan limits were being reinsured. One reason this could happen was that State agencies did not have access to the program office master loan file to detect possible program abuses, and even if they did, such access would be of limited value because the file was incomplete.

Second, the system paid lenders' bills for interest and special allowances without validating them.

Third, the system did not rebill lenders for insurance premiums when the lender did not pay the first bill.

And fourth, the system did not accumulate and report the guaranteed student loan program's financial status in accordance with the needs of the Department's financial managers.

Furthermore, we found that the Department's efforts to improve the system featured a piecemeal approach to identifying deficiencies and attempting corrections. Under this approach, user needs had not been fully identified and a system design had not been fully completed prior to beginning to build the system.

We believe the Department should first determine the extent and degree of the controls and accountability it wants to provide for this program and then adopt the systematic process specified in its own policies for the design, development, and operation of automated information systems.

This should include, first, comprehensively identifying what the users of the guaranteed student loan system need from it; then, translating such needs into design specifications.

Our report was discussed with agency officials who expressed general agreement with our findings, but stated that they had been restricted in their efforts by limited resources.

That summarizes our statement, and we would be happy to respond to any questions you or other members may have.

Mr. SIMON. Thank you very much. Let me first ask you a question that is not part of your assignment here and if I may ask you something where you are not speaking for GAO, but speaking for yourself. Obviously what Congress has intended is to provide access to higher education for all Americans who want to have that access.

My fear is that we are starting to go away from that. You have talked about collection processes and other things here, but the most fundamental question is how do we most effectively and efficiently guarantee that access to students? Now, you have looked at a variety of programs and a variety of schools.

Do you have any reflections on the broader question?

Mr. AHART. I think that is a very tough question, and I—the General Accounting Office has not made a study or reached any conclusions as an institution on what is the most effective way to do it.

So, I will speak in a personal sense in response to your invitation, based a lot on the work that I have done over the years and familiarity with the programs. As you know, up until 1958, we did very little in this area and then the national defense student loan program came to be and not much more was done at the Federal level until 1965.

Since that time, a lot of different programs have come into being, some of them much more liberal than others in terms of gaining access, some of which in my judgment were a little too liberal.

Families who could afford to put their children in college, were given the advantage of a student loan and subsidized interest rates after that, which in my own personal judgment, given the needs of this country, is not a very good way to spend taxpayers' money.

At the present time, with the amendments made this year, that has been largely taken care of. We still have a rather substantial number of programs which, again, I don't think are terribly well-articulated, one with the other, in terms of coordination.

We did have, I forget just the exact starting date, the student benefits under the Social Security Act. We studied that program and issued a report in August of 1979 suggesting that program be phased out in favor of a program which was more—in favor of a program such as the Pell grants which would more directly be targeted to those people who are not in a position to finance their education directly. The Congress has seen fit to do that.

I am not at all sure that the Department of Education and the budgetary problems has backfilled that on the other side to make sure Pell grants in sufficient amount would be available to meet the needs of those needy children who would have been eligible for social security previously, who might now resort and want to get Pell grants and guaranteed student loans and so on to pursue higher education.

I think the overall question is very difficult. I would say this: It would seem to me in the context of what we were talking about here in terms of academic progress and the default rate and so on and so forth, that we ought to couple the national desire that has been legislated in the last couple of decades to make sure that all children and students, young men and women who want to seek an education, have the financial means to do it.

We have to couple that with instilling in those same students a sense of responsibility. When they go for that kind of help from the general taxpayer, they should be, in fact, serious students and want to gain an education. Academic progress standards of the institutions which are coupled with the Federal aid program ought to insure that we do the best we can to make sure that they are there to get an education and not to spend time to do whatever they want to do.

At the same time, where the program eligibility requirements are such that children are given the advantage of loans, I think we need to do everything we can to instill in them a sense of responsibility that that is in fact a loan rather than a grant and they have a responsibility to repay that.

I think the set of programs we presently have, you could question, and people have, whether or not the amounts available under all of them are sufficient. And what should be the cut points for the availability of guaranteed student loans?

I think taken all together we have a lot of help out there for people who really want an education, particularly those that are willing to do a little to help on their own. That is a long answer, Mr. Chairman, it is a personal answer.

Mr. **Simon**. I was just probing there. Let me shift over to, first of all, the academic side. The old GI bill, post-World War II GI bill, as I recall, required a maintenance of a C average after your second year in school.

Is that correct? Or my——

Mr. **Ahart**. They had an academic requirement and I couldn't attest to just exactly what it was, Mr. Chairman.

Mr. **Simon**. As you look at—I notice you mentioned the VA program, something similar to the VA program you think should be adopted by the Department of Education?

Mr. **Ahart**. We think something similar to that should be adopted by both the Department of Education and the social security program for as long as it continues to be in a phase-out mode. Yes; we certainly do.

We don't think we ought to be putting money out, taxpayers' money out to help students who are not really maintaining satisfactory progress in the schools.

Mr. **Simon**. You say one student had been enrolled for 5 years receiving more than $4,200 from Pell grants and was academically a second-quarter sophomore. It was a whisper, he says it must have been a football player, I am sure from Minnesota, not from Illinois.

Mr. **Ahart**. I think he would have lost his eligibility after 4 years, though, Mr. Chairman. I might mention we do have just an awful lot of examples of cases which I found quite shocking when I saw them and, if a few of the members would be interested in hearing some of them, just to perhaps get a better perception of the kind of things that were going on in these schools, we would be happy to detail them for you.

Mr. **Simon**. Rather than detail, what percent would you say of those receiving assistance fall in that category, from your study?

Mr. **Ahart**. As far as the low grade point averages, I put it in the statement, some indicators of that, about 20 percent of the Pell grant people were below a C average and I think—I forget the other percentage that was involved of the social security students, a lesser amount.

It is much more difficult to determine the academic progress part of it. You almost have to look in detail at the person's grades and how long they were in school, the individual records, which is what we did to get some kind of a sense of what was involved.

And the same is true about the nonpunitive grades which people received. We had schools that followed the policy that people could withdraw from a course even after the final exams without any detriment to the grade point average.

So when you look at grade point averages, you have to do that with the understanding that depending on the school's policies, there may be an awful lot of courses which the student actually attempted and did not complete and was not successful in, that did not enter into the computation of their grade point average.

Mr. **Simon**. Would you care to characterize the institutions where you found this—I gather from your testimony that there was a great disparity in institutions on this. Would it be true, as I would anticipate that schools—for example, I am from a rural, poor area, and schools that deal with rural poverty or inner city poverty have greater problems than those, say, such as the University of Illinois, which deal with a more affluent, more articulate group financially and academically?

Mr. **Ahart**. I am not sure our study was designed to be very discriminating in that aspect. We did find problems in all different types of schools, in varying degrees. I would like to ask Mr. Fulton, who was in charge of the study. He is from our Atlanta regional office, and can give you some insight on whatever you would like—what he thinks we could characterize along those lines from our study.

Mr. **Fulton**. As Mr. Ahart said, there is no way to characterize any particular type of school. We found the greater problems in those schools that had open admission policies and didn't have restrictions on the types of students they were taking in.

That would not necessarily mean that they were rural students or poor students, but we did not—for example—go into schools such as the Ivy League schools and those which have admission policies which by their nature are designed to take a higher percentage of highly qualified students.

Most of the schools that we saw that had a significant problem had virtually an open admissions policy and had a policy that opened their doors to students that had had problems even at the high school level.

Some of these schools might have also been in the TRIO programs, the special services programs, or may have had special studies program or regional programs of their own that they were offering at these schools.

It is interesting to note that our statistics and grade point averages leave out those students who had taken less than 20 hours, because we tried to take out the imbalance of getting figures that would catch those students who had gone into the wrong school and the wrong programs.

We are dealing mostly with sophomores or second-quarter freshmen.

Mr. **Simon**. If I may shift over to the NDSL default rate, the administration is proposing that all schools with a 25-percent or greater default rate, which is about 800 institutions, currently, would not be eligible for additional NDSL funding.

From what you have observed, to what extent are we going to be punishing students rather than institutions?

This is my concern, here.

Mr. **Ahart**. I think that is hard to determine. We did, of course, in our work suggest that there be a threshold established and an institution who ran their program in a way where the default was above whatever threshold was established be denied the opportunity of further participation in the program.

In doing that, I think we recognize that the national direct student loan program is not the only kind of aid that students can get. There is still the Pell grant, there is still the guaranteed student loan program for the students eligible for that, perhaps work study and other things.

I think it would be difficult in the case of students within a particular institution to make a judgment that they were—the extent to which they might be penalized. They might end up paying more interest if they go the guaranteed student loan route, for lack of availability of the NDSL loan. These programs might have some influence on the eligibility or amount they could get out of the other programs.

I wouldn't want to assume that the students would be deprived entirely of a means to go to that institution, merely because the institution was disqualified for further participation in the NDSL program.

Is that a fair statement, Mr. Schnupp?

Mr. SCHNUPP. Yes, sir.

Mr. SIMON. Mr. Weiss?

Mr. WEISS. Thank you very much, Mr. Chairman. Mr. Ahart, in coming to your conclusions and recommendations, had you discussed them with the educational community at all before putting them down and finalizing your decisions?

Mr. AHART. Are you talking——

Mr. WEISS. The educational standards aspect of it really.

Mr. AHART. We had discussions with the schools we have visited. Let me ask Mr. Fulton to comment on the extent we may have discussed the recommendations with a larger representation of that community?

Mr. FULTON. At each of the schools visited, of course, we discussed not only the significant findings at the individual school, we also discussed the larger ramifications of it and what they saw as being problems in this area.

I guess our primary contacts, were the National Association of Student Financial Aid Directors and also the American Association of Registrar Admission Officers which together have written up a set of proposed regulations, self-regulatory guidelines for academic progress.

We had discussed those just in very general terms because our report was in process at about the time they were coming out with their standards.

And in many of the things that we were seeing in our report, they go hand in hand with the items that they covered in their guidelines. So we did discuss our standards and our proposals with everyone represented in the community.

Mr. AHART. I might mention along those lines that the statement I have seen from the American Council on Education, which lays out guidelines that it suggested schools use, did reference our study in support of the need for the academic community to better self-regulate themselves in this arena of academic progress.

So I think there is not disagreement between the academic community and ourselves on the need to do a much better job in this area.

Mr. WEISS. Given that, it seems to me that there may be a significant difference between a self-guide system and a mandated system in the Federal Government. It seems to me that that would run counter to our concerns historically about not having the Federal Government through the guise of providing opportunities for youngsters to attend college, or older people, getting in control over standards, academic standards and curriculum and all of the other problems that educational institutions have been concerned about over the years.

And do you not see that this, in fact, may possibly take us in that direction?

Mr. **Ahart**. I suppose that you could see some kind of a danger there. At the same time, I think that the Veterans' Administration's experience where they do let the institutions develop their own standards, they do look at those standards to see whether or not they are reasonable, whether they are real, that they really have some meaning to them, and they approve them, they still leave the initiative with the academic institution to develop the standards.

I think the testimony last week by the Department of Education before this subcommittee suggested that they would adopt a similar approach requiring the schools to adopt a set of standards, at least as stringent as whatever their accrediting agency has suggested as standards.

If they didn't, then they would suggest, require that they adopt ones which were in keeping with statements such as the one put out by the Council on Education.

I think that there is a dual thing that needs to be considered here. I think there is a responsibility on the part of the Federal Government in using the taxpayers' money for these aids to make sure it is a real educational experience and that people are really getting an educational experience if they are using taxpayers' money to do it.

On the other side is the thing we almost all hold sacred, to have academic freedom, and have schools in charge of their own educational programs. Those two come together and obviously you can raise and I can raise in my own mind some possible conflict between those two.

If we try to get into stringent standards and have those standards such that they are controlling the academic curriculum, there could be problems.

What we had in mind in our report and what the Council on Education had in mind with itself, and what the VA has in mind and has been doing for a number of years, is not to interfere with the structure or content or what that academic institution is offering, but to make sure that when we are providing financial aid it isn't just the student showing up at the door and spending time there and is entitled to taxpayer help.

That is where it comes together. Obviously, there is—you can pose some danger there, but I think if it is administered correctly, I don't see any difficulty. I don't see that the academic community is working on a different wavelength.

I think they see a need for better self-regulation.

Mr. **Weiss**. I think you indicated in response to a question of Mr. Simon's that about 20 percent of the schools were—correct me, that is my recollection, 20 percent of them, in fact, engage in less than strict adherence to academic standards for such students. Is that true?

Mr. **Ahart**. No, the 20 percent was the number of students that were recipients of Pell grants that fell below a C average. The percentage of the schools that we looked at, that either did not have adequate standards in our judgment or which did not enforce the standards they had was much higher than that.

I think 10 out of the 20; is that right?

Mr. FULTON. Nine out of the 20.

Mr. AHART. We found they weren't fully enforcing those that they had.

Mr. WEISS. Now, again, I think you indicated a word of caution at the beginning that you had made judgmental decisions in selecting the schools that you had gone to study.

Mr. AHART. We looked at 20 schools in 12 States. You cannot project the results of our sample to the Nation and say that is representative of all of the schools. But within those schools, we randomly sampled the students, so you can project the results of our review of the individual students referenced to all of the students at those 20 schools.

Mr. SIMON. Would my colleague yield at this point?

Mr. WEISS. Yes.

Mr. SIMON. Did this include proprietary schools?

Mr. AHART. It included schools of all types, proprietary, State-run, community-run, all different types.

Mr. WEISS. Again, it seems to me that in order to have some kind of valid idea, on this side of the table as to what the extent of the problem is, how many—what percentage of the academic institutions of higher education we are talking about, we ought to have some idea as to what those 20 schools and the 9 of those 20 schools really represent.

If you projected them across a broad range, would it in fact mean 45 percent of all of the schools across the country are having those problems? You say no, you can't do that, does it then come to 3 percent? You ought to have some idea as to what the extent of the problem is, if we are going to be adopting some cures which may or may not be appropriate, depending on what the extent of the problem is.

Mr. AHART. Let me clarify what I did say. We cannot project it scientifically. At the same time, we did make a judgmental sample, basically in that we tried to include in our sample the 20 schools.

We tried to include schools in different geographic parts of the country, different types of schools in terms of whether they were State schools or private schools, proprietary or otherwise.

We tried to design our sample judgmental to the—to be as near as we can tell without doing a scientific sample for you, such as taking a look at 300 schools, to be fairly representative of the universe.

What we come up with—you can use your own judgments by looking at the schools we went through and we will be glad to tell you how we selected them—we are talking about more than 3 percent of the schools having problems.

We are talking about probably somewhere in the ball park of what we found, a significant number of schools that do have the kinds of problems that we came up with. Whether it is 45 percent or 50 percent or 60 percent or 35 percent, I don't know.

But certainly, in that range.

Mr. WEISS. That is—regardless of who ultimately sets down the guidelines, that is a fairly shocking indictment of the higher educational system of this country, isn't it?

Mr. AHART. I think it has certainly been demonstrated to us and I think it demonstrated to the American Council on Higher Education that the academic community needs to do a much better job of developing standards and policing those standards, a much better job of self-regulation, yes.

Mr. WEISS. Then, the only other area that I want to touch on, Mr. Chairman, when we had first listened to the Office of and Department of Education about their setting up a private referral system for collection agencies to collect on defaulted loans, the argument as I recall was not that necessarily those private collection agencies would do a better, more effective job, but that they would do at least as good a job and since it is about equal, why not have the private sector do it rather than the Government hiring additional people to do it?

Now, as I understand your testimony, you are suggesting on the basis of at least some experience, that it may not necessarily be so that the private sector collection agencies can do at least as good a job as the public sector, that is the Government, in collecting on those defaults.

Is that an accurate recap?

Mr. AHART. I don't think we are saying one way or the other. What we are suggesting is that as they go forward to the contracts which I understand have already been let and they turn loans over to the contractors, that they monitor the experience they have and make a judgment down the road as to whether that is the most cost-effective way to do it.

I don't think we can answer straight out. There is one region, the San Francisco region, which did an exemplary job of collecting these loans. It was outstanding in terms of the other regions, much better than the other regions, and it may well be that whether used by private collection agencies or by the regional offices, the techniques that they used could certainly be emulated.

Now, all we are suggesting is that they track their experience, keep track of it and validate it, if they made the right judgment fine—or if not, reconsider. It is a difficult thing to measure. I think as we pointed out the studies that were made in some respects were faulty, I think necessarily so. You can't be absolutely sure which is going to do the better job or most cost-effective job, particularly in this case where the ones turned over to the private collection agencies are ones where you have already failed to collect.

Somebody has already failed to collect. They failed to collect at the school level before they get turned over to the Department. Perhaps someone failed to collect them there before they get turned over to the private collection agencies. In any comparison, you have to give consideration to the possibility, at least, a strong possibility that the difficulty of collection for the particular universe of loans is going to vary depending upon the age of them and who tried to collect them before.

So it is a tough one. All we are doing is suggesting that they monitor and assess their experience under the contract mechanism.

Mr. WEISS. Is there any special reason why the San Francisco region was able to do such an outstanding job? Were they an aberration?

Mr. Ahart. Let me ask Mr. Schnupp to comment more specifically on that.

Mr. Schnupp. Sir, we had talked to officials at the Department of Education and asked them why San Francisco was better. They advised us that they had not made any studies of the collection activities out there but they did say that they felt that the collectors out there were a better group of collectors overall.

They were able to train the collectors much sooner than some of the other regions. The support systems were much better in that region which aided in the whole process of collecting the defaulted loans turned over.

Mr. Weiss. I don't understand what that means.

Mr. Schnupp. They had an ADP system in place earlier in San Francisco, so rather than having to do a lot of manual handling they were able to use part of this system to aid in the collection of the defaulted loans. They were able to send out demand letters.

Also, I believe that one of the things that happened in the San Francisco area was that there was a U.S. attorney who was involved in taking a number of cases to court. This was highly publicized and they believed that this also probably had an impact on collections out there.

Mr. Weiss. We have been hearing over the course of the last couple of years about how the Japanese in some way are able to get more out of people who work in their industries than we or the rest of the world. I thought maybe we would come up with an area of the United States where the Federal Government can get more work out of its employees. But that is not what you are telling us?

Mr. Ahart. I think just to sum it up, it sounds like it was a better run operation, with people really giving some thought to the different ways, the different techniques they could use to improve collections, in contrast to some kind of innovations and initiatives that were not taken in the regional offices, that is what it seems to me.

Mr. Weiss. GAO comes up with no recommendations. You don't suggest that we in fact try to replicate that. We are going to ignore that as being an aberration.

Mr. Ahart. We suggested that they do consider that, that the Department of Education in assessing the experience under the contract mechanism, give consideration to the San Francisco record and to the techniques that they used there and try to capitalize on those as much as they can.

Mr. Schnupp. If I may add, that was part of our recommendation that they study the San Francisco operation.

Mr. Weiss. Thank you, Mr. Chairman.

Mr. Simon. Mr. Erdahl?

Mr. Erdahl. Just to follow up on our colleague from New York, I would think that there seems to be some techniques that would be transferable, because as you told us today, and we heard before about the default rates there is a wide disparity in different schools and different parts of the country.

That brings to mind the question who is responsible for the collection of the loans, for the student is responsible. Who is the right agency?

Mr. **Ahart**. The responsibility is with the schools that administers the program of the loans for that school. It is their basic responsibility. When they have followed through and tried what they are supposed to try and failed, they are allowed after 2 years to turn them over to the Department, and the Department then takes the responsibility to collect.

Mr. **Erdahl**. Isn't that 2-year default period or grace period too long.

Mr. **Ahart**. Some people suggested to us that it was.

Mr. **Erdahl**. I would think it would be too long.

Mr. **Ahart**. You have a tradeoff to make. If the prime responsibility is with the school, I don't know what the judgment would be as to how long we have to hold them to carry out the responsibility before we take over that responsibility from them.

If you allow them to make one try, and if they didn't get paid, turn it over, the Federal Government would be involved in all of them. I don't know what the right cut point is. Maybe it should be earlier and again, we suggested the Department of Education consider that and if they feel it would be advantageous to allow turnover under certain circumstances, that they propose legislation which gives them that flexibility.

Mr. **Erdahl**. One of the institutions in our country that does a rather good job of collecting loans are the banks. Shouldn't the banks and financial institutions have some responsibility in collection? It seems to me that they have a guarantee. We have a banker yesterday and he implied that it wasn't really a professional concern, it was a concern of his as a taxpayer and individual. But whether or not the student paid the loan back, they had a guarantee so the banker always got his money.

It seems to me that we could put some accountability in that area as well. Would you comment on that?

Mr. **Ahart**. Well, in the guaranteed student loan program as distinguished from the National——

Mr. **Erdahl**. I am talking about the GSL.

Mr. **Ahart**. Under GSL, the prime responsibility is with the lending institution to effect collection and they do have I think a somewhat better record than the national direct student Loan program. But in the final analysis those are insured loans.

I think most banks follow their ordinary thinking because perhaps the Federal guarantee does not follow quite as far as they would if they were not guaranteed. But they are, and in the final analysis they can turn those over and collect the insurance on them if they fail to make the collection in the normal course of business.

Mr. **Erdahl**. It also seems reasonable, as you have told us and your colleagues here, that we have some responsible standards. I think you cited what the Veterans' Administration has done and Chairman Simon mentioned about the GI bill. You bring up these rather large instances.

I wonder how really typical they might be of some person taking a course—I think one in your report took an accounting course five times. Either that person should have gotten an A for tenacity or maybe he had an awful pretty teacher. I do not know. Whatever it may be, it seems to me that is an abuse of the system.

We talk about some schools being selective, they take only the top students in the first place, some of the private colleges do that, others I guess give the kids a right to flunk, give them a chance.

I kind of like that idea of open enrollment. But how long do we go, past the sophomore year or something? It seems to me we should expect some type of a uniform standard to see that these people are not professional students. That is not what the program was intended to be. I think your points on that give us a challenge we should work on.

Also, in another area you mentioned about contracting out to collection agencies, and also I believe you mentioned, Mr. Ahart, that a certain number, if we use a term around town, in the area of collection, were being RIF'd.

What is this number you said, personnel going from 900 down to 400?

Mr. **Ahart**. We are going down from 900 to 250, I believe.

Mr. **Erdahl**. Would that slack be made up by contracting these out to the collection agencies, to the bill collectors?

Mr. **Ahart**. Basically that is the case. It would be a function to be done in the private sector under contract.

Mr. **Erdahl**. I know there is a great impetus in this town to do everything in the private sector. But it seems to me as you have told us today, we have had examples in the west coast, the San Francisco office, we have some information about schools having records of 5-percent defaults, others over 41 percent, so obviously the techniques, the mechanism is there.

I just wonder, as a Federal agency, if we are being penny-wise and pound-foolish. Going back in this area, personally I have a little difficulty—I speak as one member of the committee—saying we should turn this over to some collection agencies. Some of them are obviously very responsible. All of us know I think others have acted in an unresponsible, threatening, harassing way. I am not sure our taxpayers should be funding that type of operation. I am not trying to impugn collection agencies as such.

Mr. **Ahart**. I am not personally familiar with the contractual terms, in terms of how these collection agencies need to continue themselves to carry out this function. I would assume that the contract—Mr. Schnupp might have some comments on it—that we are getting responsible contractors to carry out this function. I think it is a judgment and obviously it is between different philosophies as to how many functions and what kind of functions ought to be done with Federal employees as opposed to being done under contract.

I certainly do not want to referee that one. That question has been around for a long time. Sometimes cost is the very basic consideration, sometimes it is not as important a consideration. In this particular case, contracts have in fact been let. They were let in December. I think last week they started turning the cases over to them.

Mr. **Erdahl**. If I could interrupt, what percentage is the norm, if you are aware, what percentage under contract does the collection agency keep? Do they keep a fee, a certain percentage?

Mr. **Ahart**. They do. This is contracted for each of the three regions separately, the three regions that are the collection points.

In one of those contracts, I think the amount is going to be 38 percent; the other, I think it is going to be around 24 percent. That will be the amount which will be kept by the collection agency to reimburse them and compensate them for their services.

I think the Office of Education has come up with a kind of average number of around 29 percent for all of the contracting together.

Mr. **Simon**. If my colleague would yield?

Mr. **Erdahl**. Of course I yield to the chairman.

Mr. **Simon**. I think, in fairness to the department, we have created this problem to some extent. We mandated when we created the Department of Education that they had to get rid of 500 employees and they had to look around "Where can we get rid of 500 employees?"

Mr. **Erdahl**. And they hire 500 consultants.

Mr. **Simon**. Well, that is your comment, but I think we put the Department in a very awkward situation. My guess is we might meet with the leaders of the Department and privately they might very well agree with the sentiments being expressed around here. But they had to make a choice of where they were going to get rid of some people. Even though other people are put on on a contractual basis, they had to meet the legal obligation.

Thank you.

Mr. **Erdahl**. Thank you, Mr. Chairman, for sharing that. I think it is a valid point.

One more question. I do not know if it comes into any of your reports here, Mr. Ahart, but we have heard, and I am not a lawyer familiar with all of the ramifications, but what about using the IRS as a collection agency, if I could use that broad term to describe them, sometimes?

Mr. **Ahart**. Well, I do not know whether you would want to get the IRS into the business of collecting student loans.

Mr. **Erdahl**. I do not mean about collecting them, I mean provide the information on students.

Mr. **Ahart**. We have had discussions in the past, I think some programs do use it, are authorized to use the IRS as a locater, in other words, to find out where a person is. I think some use has been made in the past, I am not currently familiar with exactly where that stands. Perhaps one of my colleagues does with respect to the student loan programs.

With taxpayer information, the Congress has always had the attitude that taxpayer information as such is very privileged data. I think that is correct. Everybody tends to resist, properly so, using the tax-collecting mechanism as a means to get at a lot of other kind of problems they would like to get at.

I think Congress should be wary of allowing access to this program or that program. I think in some cases it makes a lot of sense where someone owes the Federal Government money, they would be able to find out where that person is.

Mr. **Erdahl**. That is my point.

I think we do get into a dangerous area if people get some assistance, tax refund, and we say you are getting a refund and you also owe the government a student loan. Some people say let's get at it that way.

I have uneasy feelings of where that might lead. But I think as a locater some of these schools, most of us have gone to a school or two, they keep track of the alumna when they want donations to their school.

Mr. **Ahart**. Mine do.

Mr. **Erdahl**. I would think they would keep track of their graduates for purposes of collecting as well.

Thank you very much.

Mr. **Ahart**. Part of that, if I might just comment, part of that is a problem, some of the schools are a little bit reluctant about letters to alumni from whom they are also trying to collect donations.

Mr. **Erdahl**. Thank you.

Mr. **Simon**. Mr. Peyser?

Mr. **Peyser** Thank you, Mr. Chairman.

Mr. Ahart, in one way the testimony that you have given in written form is disturbing, and I think that is your job basically, as long as it is accurately reflecting a condition that exists in the country on this matter of both adequacies of educational requirements being met, to report repayment of loans, and the losses to the Government.

You have made certain judgments on this, you say, and I would like to be able to make the same judgments as you did.

I would like to, first of all, know what schools were involved in this process.

Mr. **Ahart**. We can detail those. They are listed in our report.

Mr. **Peyser** Is that report available right here with the list of other schools? I did not see it.

Mr. **Ahart**. I can show you a copy.

Mr. **Erdahl**. If the gentleman will yield, I was also looking partly out of curiosity. You mentioned some midwest schools had a pretty good record. I was curious which ones they were. I did not find it in the report.

Mr. **Peyser** I am hopeful we are going to get that. I did not see it either.

Mr. **Ahart**. On the academic progress standards report, we do list the schools in the report, on page 31 of that report. I do not know if you have it there. We list the seven 4-year public schools, 4-year private schools; six 2-year public schools; one 2-year private school, a public vocational and a proprietary school.

If you like, I can read those out or you can glance at it.

Mr. **Peyser** This is on page 31, "Institutions Visited During Review."

As I am making a rapid run through this, I find it hard to believe, but I do not see any northeastern schools listed at all here. Is there any partcular reason there is no school from the Northeast?

Mr. **Ahart**. Let me glance down the list. It does not appear any of them are in the northeastern part of the country. There are some in the Eastern site. I guess the closest one would be——

Mr. **Peyser** As I am looking I see Alabama, Idaho, Kentucky, Florida, Georgia, Illinois, Georgia, Missouri, Ohio, Florida, Oregon, Ohio, Illinois, South Carolina, Indiana, Georgia.

Georgia wins the ball game as far as the number of schools that you have looked at in doing this program.

First of all, I am wondering how do you take this as a representative listing around the country? I see practically no western schools, no northeastern schools, and I am wondering why this is the kind of list you think is appropriate.

Mr. **Ahart**. We tried to get schools representative by type of school, we tried to get some geographic dispersion, although if you are only going to pick 20 schools, it is hard to get a sample that could not be quarreled with.

One of our considerations was obviously the economy of making the study itself. We did have the Seattle office involved in the study, out of our regional office.

Mr. Fulton was one of the principals. There was a tendency to try to minimize our travel costs as well in visiting these schools, and so on.

I would if you like, Mr. Peyser, ask Mr. Fulton, who was involved in the study design and the sample of the schools, to detail for you the considerations and why we feel it was a useful judgmental sample in terms of trying to get a sense of conditions, even though we readily admit it was not a sample that was scientifically designed so that we could project the results with scientific validity to the nation as a whole.

Mr. **Peyser**. I am having a problem with this, because what you are saying, I can just see the report in the media of a condemnation of these programs based on schools that are not paying any attention to educational requirements when you say under the Pell grants 20 percent of the Pell grant recipients and nearly 45 percent of the schools are not really paying any attention to academic requirements.

I looked through this and I find, for instance, in the 2 year public schools and private schools nearly 50 percent of them are southern schools in just three districts. Now I do not think—in fairness, Mr. Chairman, I think that this kind of a report that is as sweeping in its statement as it is, that is confined to such a really comparatively less than half of the representative schools in this country in just my geographic area, really raises the question as to the validity or how much attention should be paid to this. And it is disturbing to me.

I am delighted to know New York schools are not listed here. I am sure some of them have problems. I would like to know about it, but I would have to raise a serious question on this type of a report and I think any person in the education community looking at this report would have to really raise the same kind of questions based on the schools you visited, the areas that they ran and the types of schools they are and, based on that, to pass a judgment on all schools.

Now, this list refers I gather to these schools here, just to the academic requirement question?

Mr. **Ahart**. Yes.

Mr. **Peyser**. Not to the repayment question or not to any of the other areas?

Mr. **Ahart**. Yes.

Mr. **Peyser**. So we do not confuse this at all, if you are dealing with a guaranteed student loan section, you have raised some serious questions there also on the guaranteed student loan.

Mr. AHART. We are talking about the national direct student loan?

Mr. PEYSER. No, I am talking now guaranteed student loan.

You also have a section here dealing with the guaranteed student loan. In your report you speak of the guaranteed student loan as well as the national direct student loan.

Mr. AHART. Are you talking about the academic program?

Mr. PEYSER. I am talking about your statement this morning that incorporates the guaranteed student loan as well as the others.

Mr. AHART. As one of those programs where academic progress standards should be in play, yes?

Mr. PEYSER. That is right.

Also, you make reference to the repayment situation in the answer to the question, just given a minute ago, you stated that the guaranteed student loan repayment was somewhat better than the national direct student loan.

Now do you have the default rate on the guaranteed student loan in the last academic year?

Mr. AHART. Let me ask Mr. Schnupp if he has it with him. If not, we can obtain it for you.

Mr. SCHNUPP. Yes, I have seen default rates in their budget justification for 1982. It is broken down by both the federally insured portion of the GSL program and the State guarantee agency program, where most of the activity is now. What they show is a 14.5-percent claims rate.

Mr. PEYSER. That is right. That is not a default rate.

Mr. SCHNUPP. No, sir, that is the number of loans turned over to the Department of Education for collection. They show a default rate I believe of a little bit less than 9 percent.

Mr. PEYSER. That is correct. We had actually an 8.3-percent figure as the default rate. Now in your testimony you show that the national direct student loan default rate was 16.2 percent. So once again for the record I think it is important that we have a little bit better default rate. It is 100-percent better.

In other words, if you want to look at it that way, it is 8 percent as against 16 percent in the guaranted student loan. So I think it is important because there has been a lot of criticism out there that the students do not repay their loans under guaranteed student loans.

The facts are now showing us they are repaying their loans at a higher rate than commercial bank loans are being repaid in this country. So I think it is a very positive statement and I do not want it to be construed as a negative one by your inferring that it is somewhat better. It is a hell of a lot better. Frankly, it is going to get even better as we go along.

Now, on the guaranteed student loan on the academic information, do you have information in there then on the academic requirements being met by those on guaranteed student loan.

Mr. AHART. I am not sure we have that broken out separately. We had it broken out in terms of the Department of Education programs, of which the guaranteed student loan would be one, and the Veterans' Administration students and the SSA students.

Only some of these students get help from more than one source. They might have a Pell grant, they might be getting VA benefits, as well as have a guaranteed student loan. So it is very difficult to make distinctions on the academic standards between those.

But let me ask Mr. Fulton and we will do what we can.

Mr. **Peyser**. I would like to qualify that a little. I would be interested in knowing, for instance, students on the guaranteed student loan who have no other benefits as to what their academic information in meeting those academic requirements would be and those that are guaranteed student loans with other benefits.

Maybe there is something to be learned in that situation, because the problem I have with this report, one, as I have mentioned, is the selection of the schools and the geographic distribution and types of schools; two is a broad brush that seems to implicate all of these areas under the same problems and I do not think they are under the same problems at all.

I think in close examination, we already know that the repayment rate does not at all coincide with the national direct student loan repayment rate or the default rate. I think we would also find out that the problem you are citing, and I think it is a problem that ought to be addressed, dealing with the schools not paying any attention to academic requirements and the results of the Pell grant students as well is sort of being rolled into the whole program dealing with guaranteed student loan as well, is a very misleading thing.

I hope that the media will very clearly define the differences because with the administration's present effort of basically slashing the guaranteed student loan, eliminating graduate school students from even qualification, all gets tied into this kind of a report, which sort of says they are not entitled to it. "Look at what they are doing."

So I, one, would urge that this report be viewed, Mr. Chairman, in a very qualified way as being very limited in its scope and very limited in its area that it is reaching. Also we have to be very sure that these areas that we are discussing are separated and not rolled into one package as this whole student aid program is sort of a disaster, because I do not believe it is. And at that point I will yield back my time.

Mr. **Simon**. Thank you, Mr. Peyser.

If I can just follow through and let me say we are grateful for the contribution that you have made, I think it is a significant contribution. I do think my colleagues make a point that we should be cautious about generalizing.

If I can have your attention, Mr. Peyser, I note the three schools in Illinois all serve the East St. Louis, Ill., area, which is an area that is the most troubled urban area by far in the State of Illinois, one of the most troubled in the Nation by any statistical gauge. To generalize on the basis of three schools serving East St. Louis, you do not get an accurate picture.

Let me say in fairness to these schools they are dealing with people who need special help and special assistance to be lifted. I am not critical of those three schools when I say this, but I think we have to be very careful before we assume a national picture on the basis of those three schools, at least where I have some immediate knowledge.

Mr. **Ahart**. Could I comment on that?

Mr. **Simon**. Yes.

Mr. **Ahart**. I certainly agree with you, certainly we do not want to condemn and we did not have the intention to condemn every school in the country. What we tried to do is to pick sample schools, judgmentally, to give us a feel for what was happening in relation to the fact that we have the office of education, which in effect says you set your own standards and we do not worry about it too much from that point on.

So you can generalize in the sense that we have Federal programs which are operating which go to all kinds of different schools across this whole country, with billions of dollars going into support for the students in those schools, without a Federal presence in terms of whether the schools have academic progress standards or, if they have them, whether or not they enforce them.

Now that, I think, is the central point of our report. If we are going to have taxpayer money, Federal money support students going to schools, we ought also I think to have a Federal responsibility to see to it that the schools do have academic progress standards and in fact enforce them. Now in that sense, it can be generalized.

Mr. **Simon**. If I can just say, I do not suggest that we should not be moving in this direction. I think your report makes clear that we do have problems. I am concerned about the generalizing that may take place as a result of a report like this, that looks like the student loan and grant program, are just massively abused, which I do not believe is the case. Where there are abuses, we have to move on them.

Mr. **Weiss**. Would you yield just a moment?

Mr. **Simon**. Yes.

Mr. **Weiss**. We got into this area because I had asked, I think, as to whether any conclusions could be drawn from the 20 schools that were selected, whether in fact that 45 percent, 9 out of 20 you had said, were not adhering to their own standards.

I wanted to know whether that reflected universities and colleges, educational institutions of higher learning across the country, was that 45 percent across the board, was it 3 percent, could you tell?

I had anticipated that your response would be, because of the manner in which these schools were selected, that really they were only instructive as to the particular schools that were selected. Instead, you said that you were comfortable in suggesting that these were fairly representative of schools across the country and that you could draw the conclusion that there is the same percentage roughly, 45, 50, 60 percent, across the country of all institutions of higher learning.

Now on the basis of what has developed in the questioning since then, I wonder whether in fact you want to stick to that position, since I think I heard you say somewhere along the line that one of the bases on which the schools were selected was the ease with which people on your staff could get to those schools because of travel cost restrictions.

I heard that accurately, did I not?

Mr. **Ahart**. Yes. I think you heard maybe something I did not state, if I said it I am sorry. What I tried to say, let me play it back and see how it compares with the discussion we had.

I said we cannot, based on this judgmental sample, project with any scientific precision the degree to which the problem exists. We did make a judgmental sample, we tried to get different types of schools in different parts of the country, we did not try to get every part of the country, I did not add that before; I think we can show from the sample, and reach a fairly valid conclusion that it is a significant problem.

I went on to say that I do not know whether it would be 30 percent, 45 percent, 60 percent, based on this. But certainly it is support, at least in my mind, it is a significant problem that from the standpoint of the thrust of this report that the Federal agencies should have a means to see that the academic institutions do have academic progress standards and are enforcing them; that it certainly is valid enough and precise enough to suggest that that problem does in fact exist and, yes, in fact we should do something about it.

Mr. **Weiss**. I know, but again the question——

Mr. **Ahart**. I was not trying to suggest that 45 percent or 30 percent or 60 percent was the right number.

Mr. **Weiss**. That is a little bit better.

The framework within which I asked the question was in order for us to come up with a valid response, a valid answer. We ought to have some clear idea of the extent of the problem and I was concerned that on the basis of the information that you gave us, of these 20 schools, as given to us, did not provide that kind of specificity. And as I understand your testimony at this point, you are in essence now saying the same thing, that in fact—and correct me—this is the conclusion I draw, that before I come up with any kind of formula or regulations or law mandating anything on anybody, I would really want to know a little bit more about what is happening across-the-broad range of schools, perhaps scientifically selected, before we do that. I would like your response to that.

Mr. **Ahart**. Again, I do not think we are suggesting that the Federal Government define exactly what any one individual school ought to have. We are suggesting that the Federal Government require that the school have some standards and that they be reasonable. There would obviously be room for variation.

If you have an open admissions policy and the philosophy of that institution is to give everyone a chance to come in, certainly they would not have the same academic requirements perhaps the first years Harvard University would have to stay in that school. But reasonable ones should be set by that school.

I do not think by any stretch of the imagination you would have one that would allow somebody to stay in school 5 years and progress to the point of being a second-quarter sophomore. Now it is in that ball park someplace.

I think again in terms as I answered the chairman, I think we have sufficiently demonstrated in the educational community, who I think agrees, and the Department of Education agrees, that the problem is significant enough to worry about in the context of the billions of dollars that we are making available through the Federal Government to support students. We ought to have some assurance that the institutions do have some academic progress standards and that they adhere to those academic progress standards.

Mr. **Weiss**. I do not want to go around again. It reminds me of the story I heard when I was very young about the person who lost a nickel and looks under the street light to find it, even though he lost it on the corner, because it is brighter under the street light.

If you are going to go out and investigate schools on the basis of where your headquarters are located and where it is easier and cheaper to get to, I suspect that the answers you are going to come up with may be convenient and cheap, but they "ain't" going to be accurate.

Mr. **Ahart**. I would not want you to misunderstand. We designed the study to accomplish a purpose. The purpose was to see whether or not the problem was significant enough to worry about.

Mr. **Weiss**. OK, I agree with you. It is a significant enough problem to worry about.

Mr. **Simon**. If I may interrupt this dialog because we have some other witnesses.

Mr. **Weiss**. Thank you, Mr. Chairman.

Mr. **Simon**. We appreciate your testimony and your contributions here today. We also will be submitting some additional questions, written questions we would like response to for the record.

Dr. James J. Whalen, the president of Ithaca College of Ithaca, N.Y.

Father Weiss, if you would want to join Dr. Whalen here. Father Weiss is president of Rockhurst College in Kansas City.

Dr. Whalen, if we could hear from you first and both of you may proceed as you wish. We can enter your statement in the record; if you wish to summarize it it probably will save some time and we can devote more time to questions.

STATEMENT OF JAMES J. WHALEN, PRESIDENT, ITHACA COLLEGE, ITHACA, N.Y.

Mr. **Whalen**. Thank you very much, Mr. Chairman. I will try to be brief.

My full text has been submitted.

Mr. **Simon**. It will be entered into the record.

Mr. **Whalen**. I do appreciate the opportunity to comment on the administration of the NDSL program at Ithaca College where I am president.

I am also chairman of the board of CICU, the independent college organization in New York State and speak on behalf of them. I have filed a full and detailed statement which you indicated will be included in the record.

We at Ithaca have had a good experience in NDSL collection, with our default rate ranging from slightly above 9 percent to slightly below 6 percent in the past 5 years. Last year it was 6 percent.

The reasons for this moderate default experience are a combination of several factors.

First, we are careful in the granting of loans. Our policy is to develop individual financial aid packages which reflect the need and ability of our students. We try to reserve loan dollars for students who, though needy, are the most likely to be able to meet their obligations upon graduation.

Second, we conduct an orientation process for loan recipients that spans their 4 years of college and culminates with a personal exit interview which is required for graduation. If they do not attend that exit interview, they do not get a diploma. We then employ our computer system to promptly generate bills and payment reminders.

When a borrower is more than 90 days in arrears, we use the services of an agency specializing in debt collection by mail. If default seems apparent, we go to court, obtain judgments, and prosecute. If prosecution is not successful, we then surrender the obligation to the Federal Government in a timely manner, not years later, so that further collection attempts can be made.

Each aspect of our program reflects our belief that students have serious obligations for the repayment of these loans and that we at the institution have a responsibility to conduct the program in a businesslike manner. In general I believe that application of these steps, careful lending, borrower orientation, prompt billing, rigorous collection efforts, and a willingness to relinquish bad paper to the Government will be of help to other institutions with serious default problems.

However, there is another factor which must be taken into consideration when examining institutions with default rates, high default rates. If an institution's location and mission tend to foster high enrollment of severely disadvantaged students, default on NDSL loans will probably be difficult to avert.

The postcollege road for those who enter college with extreme economic and educational disadvantage may be difficult. Their ability to repay loans on a timely basis is often hampered by problems in obtaining employment at salaries sufficient to support them.

As you know, both the Department of Education and the Congress are now considering proposals to reduce the NDSL default rate nationally. While I believe these efforts to be extremely important, I am quite concerned with their timing and substance.

The Department of Education in early January issued proposed regulations to deal with high default rates which are scheduled to become effective at the end of March. These regulations will, if enacted, have a serious effect on many institutions. The sanctions against institutions experiencing high default include the following, if the default rate is between 10 and 25 percent: The institution's Federal capital contribution will be reduced by the percentage in default. If the default rate is above 25 percent, the Federal capital contribution will be cut off completely.

While the spirit of these draft regulations is wise, it is my view that these new sanctions should be introduced gradually. It has been my observation over the past years that attempts to pressure institutions into improving NDSL collections have been sporadic. The bark has been much more serious than the bite.

While the time is certainly here for some bite, institutions need room to plan for reduction or elimination of the Federal capital contribution. Proposing strict sanctions in January and implementing them in March seems to me to be unwise.

Further, it should be kept in mind that reductions or elimination of the Federal capital contribution are punitive in nature, but the students in default and administrators responsible for poor collection experience will not really suffer from those reductions. Those punished will be the young men and women who have not yet begun their college careers.

I have detailed my final concern with these draft regulations in my written testimony, but I would like to point out briefly that default rates are calculated on the aggregate number of dollars in default. This means that an institution can have a poor history, respond to new policy, vastly improve collections and still be many years in the process of bringing its aggregate default rate below the 25 percent required for receipt of a Federal capital contribution.

I fear that the draft regulations as they now stand would act somewhat like a debtor prison, once you get in, it is very difficult to get out.

In conclusion, I point out where, by intent or accident, over the past 20 years a variety of methods of financial assistance have been developed that speak to the variety of needs among college-bound students.

Some students are able to work and perform well academically. Others cannot do both.

Some students can be expected to obtain employment upon graduation which will make it possible to retire a heavy loan burden; others cannot.

Some students are in college because we have a national policy goal to break the cycle of educational and economic disadvantage through access to postsecondary education. These students are the target of a substantial direct investment in what might be referred to as the society's future well-being.

In education and legislation we need to be concerned about recognizing the need to employ various aid forms in this context of differing problems and abilities. As you consider these programs during the coming weeks, I hope you will not view them as a single sum of money to be distributed to college students, but that you will examine the interrelationships and the extent to which they make it possible for us to assist students in ways most likely to result in educated and productive members of society.

I would add that it seems to me that the emphasis has been placed on the defects, not on the tremendous good that has been done for the students of this country. For each student who spends 5 years obtaining two quarters, as I heard this morning, we have hundreds and hundreds of students who finish college in 3 years, doing an outstanding job.

Thank you for this opportunity to comment.

Mr. SIMON. Thank you very much, Dr. Whalen.

[Prepared statement of James J. Whalen follows:]

PREPARED STATEMENT OF JAMES J. WHALEN, PRESIDENT, ITHACA COLLEGE, ITHACA, N.Y.

I want to begin my remarks by thanking the Chairman and members of the subcommittee for providing me an opportunity to address what I consider to be an extremely important issue, the National Direct Student Loan program and its administration.

In the Chairman's letter, he indicated that the invitation was extended because my institution, Ithaca College, has a successful program for collection of National Direct Student Loans. We do have a good program and for several years have enjoyed considerable success in avoiding default by those graduates who borrowed money from the College and the government through the NDSL program.

I want to first give you an idea of what this program means to Ithaca's students. This year, we have approximately 4,500 undergraduates at Ithaca, about 2,000 of whom are eligible for NDSL's. Of these, about 700 have received National Direct Student Loans. Our loan volume for the 1980-81 year was over one half million dollars. Our average loan was $1,100 with a low of $500 and a high of $1,250. You should note that in spite of the fact that the loan ceiling was increased to $1,500 annually and $6,000 over four years, we have retained an $1,250 annual and $5,000 career loan ceiling so that NDSL dollars assist the largest number of students.

Since the program's establishment at the College, more than $10,000,000 has been loaned and $5,500,000 collected or cancelled. Our default rate for the past year was 6.63%. (I have for your convenience addended a list showing our default experience over the past 5 years.)

There are a number of factors which we consider responsible for this performance.

First, Ithaca College has approached the use of the National Direct Student Loans as a part of our financial aid package for incoming students in a very careful manner. We tend to direct these dollars to students who combine a genuine high need with a probability for academic success, special abilities and talents and a strong desire to attend the College. Consequently, these students have a high probability for success following graduation.

I do not want to suggest here that we lend NDSL funds to "low risk" borrowers in the traditional banking sense, for that is not the case.

In fact, eligibility for financial aid in most instances would suggest "high risk" in the banking sense. But we do take into serious consideration the realistic possibility that loan recipients will be able and motivated to repay. We believe that a motivated student is more likely to meet his or her obligations, whether academic or financial.

A second factor in our loan granting process has to do with the extent of a student's educational and economic disadvantage. Our most severely needy students are often young men and women who will benefit greatly from their educations but who come from families with little ability to help them following graduation. It is our belief that we should minimize the loan burden these students will be asked to bear upon graduation. Accordingly, for these students, we as a College combine direct grants, scholarships, work-study and state aid rather than relying upon substantial loans to finance their educations.

A third factor in our lending procedure has to do with personal contact between our financial aid staff and loan recipients. Throughout their college careers, loan recipients are in contact with the staff regularly and the staff reinforces the concept that a loan is an obligation which must be met.

I will turn now to the matter of collection procedures. Prior to graduation, every NDSL recipient is required to attend a personal exit interview with a member of the bursar's staff. If the student does not attend the interview, the student does not receive a diploma.

At the time of the interview, the student is advised of his or her total NDSL obligation and presented with a form showing the optional payback plans, the interest schedule and the payment schedule. The student may then choose to repay the loan on a monthly or quarterly basis. The student is required, as a part of this interview, to complete a data sheet which gives us considerable information with which to track the student in the event that he or she moves without notifying us.

Upon the expiration of the nine-month grace period following graduation, a first billing is generated by our computer. Happily, the great majority of our students respond with a check. In the instance of those who do not, a second notice is generated in 30 days and a third in 60 days. These notices inform the debtor of his or her obligations and urge maintenance of a good payment record.

If in 90 days the debtor has not responded, the account is turned over to an agency which specializes in debt collection through mail notification. A series of tailored letters, five in all, are sent at two week intervals and the last letter advises that the matter will be turned over to Counsel. (For your information, I have addended copies of the billing notices, agreement data forms, and letters of advice to this testimony.)

If this procedure does not yield payment or an arrangement for payment, we then proceed with formal legal action. In New York State, College Counsel handles litigation. Outside the state we employ the services of a collection agency. We are quite serious about this process. For example, our controller advises me that he signed four judgments against graduates in default last week.

This entire process is handled through the Bursar's office and is largely mechanized. We employ one clerk and a few hours of student help to conduct collections. The cost of routine account maintenance is about $20,000 per year. The cost for collection of accounts in arrears varies with the circumstances.

It should also be noted that in accordance with the Federal legislations establishing NDSL, institutions are permitted to surrender accounts in default to the Federal government for collection. The rationale for this is that the government may be more successful than the institution at collection. To do so however, removes the loan revenue from the institution's "loan pool" for future use. There is some reluctance, I believe, on the part of some schools to surrender this "bad paper" in any quantity, thereby reducing their loan pool permanently. We, however, believe that our collection procedures are such that by the time surrender of the obligations to the Federal government takes place, our probability of collection is quite low. We also feel that the students in default should not be permitted to abrogate their responsibility to pay. Once our approach is unsuccessful, we believe the government should have the opportunity to collect. In recent years, we have surrendered more than $108,000 in defaulted loans to the government, which is also a contributing factor to our relatively low default rate.

Now, I would stress here that in the opinion of our controller, financial aid officer and bursar, the rigorous collection process is not the only variable responsible for our respectable default rate. We believe that our success is the result of the three elements of our program: first, careful utilization of loan funds at the outset; second, the establishment of clear expectations at the time of loan and upon graduation; and third, a prompt billing and rigorous collection procedure.

I am convinced that some of the problems faced by institutions with high default rates can be successfully dealt with through improvements of each of these aspects of their program. But I am also concerned that some institutions, because of the nature of their student populations, will encounter problems regardless of the adequacy of program administration. If the great majority of a student population is severely educationally and economically disadvantaged, then the default rate within that population is going to be extremely difficult to control. This is a standard argument, not because it is easy to make or intended to play upon your largesse, but because it is a reality. Expecting an inordinately disadvantaged group of people to "make good" on monthly or quarterly payments when employment is difficult to obtain, unemployment extremely high, and entry level salaries low, seems unrealistic.

I would like now to turn my thoughts to the matters of future Federal policy with regard to NDSL collections, and in particular, to methods recently proposed to deal with institutions which do not enjoy the success rates Ithaca has experienced.

As I know you are aware, considerable attention has been focused on high default rates at institutions throughout the country. I believe that this attention is warranted and I believe it is incumbent upon both governmental and institutional leaders to do something about high default rates. I am, however, quite concerned about the manner in which this problem is to be addressed.

Last month the Education Department issued draft regulations intended to deal with the question of high NDSL default. These draft regulations reflect a bill introduced last session by the Honorable Mario Biaggi. The provisions of both the draft regulations and Congressman Biaggi's bill are intended to solve the default rate problem. Simply put, if an institution's default rate is in excess of 10% but less than 25% a reduction will be made in the Federal Capital Contribution to their NDSL fund for the current year in some proportion of their total default rate. If an institution's default rate is in excess of 25%, that institution will receive no Federal Capital Contribution.

I have two problems with this approach as a method of resolving the default rate problem. The first has to do with just who is actually punished by such action. Individuals who are in default and institutional leaders who have tolerated high default rates will feel a "ripple effect" from these measures. But the brunt of the punishment will be felt by young men and women who have not yet entered these institutions and who, if properly selected and advised, may be genuinely willing and able to repay their loans. It appears to me that we may well be punishing the wrong individuals with such an approach. This is particularly concerning when we know that reductions in available grant-in-aid monies are certain to take place. It would seem more responsible to expand and properly administer a self perpetuating loan program and make it just that, self perpetuating.

A second matter of much concern to me in the proposed regulations has to do with the timing of their introduction and the formula for their implementation.

I recognize that for the past several years, the Education Department has been struggling to resolve the high default rate problem and has given considerable warning to institutions and effected some sanctions at institutions with inordinately high default rates. But my observation is that the enforcement of sanctions has not been rigorous enough to have made "believers" out of many college administrators. While it is certainly time to "get serious" about defaults, new sanctions should be introduced in a time frame which permits institutions likely to suffer major reductions or cut-offs, an opportunity to determine how they will handle such changes in aid availability. To announce such sanctions in January and implement them in March seems most drastic.

The formula for sanctions in the draft regulations also seems quite problematic. Institutional default rates are calculated on the basis of the aggregate number of dollars loaned which have come due, in relationship to the aggregate number of dollars in default.

An institution may have experienced several years of high default rates and that same institution may have also addressed the problem seriously and made major headway toward better collection. But within the context of the aggregate numbers, the institution could be several years without further Federal Capital Contributions under the proposed formula.

Suppose that Ithaca College had loaned $400,000 over the past ten years and had $160,000 in default. The rate of default would be 40 percent. Then, suppose that Ithaca revised its policies and procedures and in the following year on $40,000 loans coming due, reduced its default rate to only five percent. The aggregate default rate despite the improved performance, would be 36 percent. If, for the next five years, $40,000 came due each year and the average default rate over the six-year period was only 5 percent, the aggregate default rate would remain at 28 percent, given the method of calculation. Despite vastly improved loan collection procedures and experience, the institution would still be denied any Federal Capital Contribution. I trust you can see that such an approach warrants some very serious discussion before it is enacted. In my view, it is somewhat reminiscent of the ancient debtor's prison. You couldn't get out until you paid your debts, but you couldn't pay your debts while you were in the place because you couldn't work.

In summary then, we at Ithaca have been successful because we have been thoughtful in granting loans, thorough in our orientation of loan recipients and vigorous in our collection procedures. I believe these approaches will be of some help at other institutions but I do not believe they are an answer for all institutions. I would call upon this committee and other members of Congress and the Education Department as well, to remember that no two educational institutions, like no two constituents, are exactly alike. We have different student bodies, draw from different communities of vastly different natures, have different fundamental missions and very different histories.

While steps must certainly be taken to resolve the default rate problem, I urge all involved to take those steps in a thoughtful and cautious manner so that we do not punish future students for the sins of past students and administrators, and so that we do not build mechanisms which will deny much needed resources to institutions which have done poorly but are genuinely improving their performance.

Again, my thanks to the committee for its consideration of my remarks.

ITHACA COLLEGE

NATIONAL DIRECT STUDENT LOAN PROGRAM

DEFAULT RATE

1977	7.41%
1978	9.24%
1979	5.81%
1980	6.63%
1981	7.54%

NDSL BILLING MESSAGES

First Payment Notice

The first payment on your student loan will be due in 45 days. Review statement and enclosure carefully to ensure that you receive the full benefits allowed.

Current

An additional months interest will be charged on all payments received after (date) .

30 Days Past Due

Delinquency Notice: You are presently delinquent on your account. Please pay the amount of this statement.

60 Days Past Due

You are presently 45 days delinquent on your account. If payment is not received within 15 days, a hold will be placed on all requests for information from the College, on your academic records, including requests for transcripts.

90 Days Past Due

United Compucred Collections five letter program

ITHACA COLLEGE

Date: April 20, 1981

To: NDSL Borrowers

From: Jean A. Hamill Jean A. Hamill
Bursar's Office, NDSL Section
Phone: 274-3132

Re: NDSL Exit Interview Meetings

Our records indicate you are scheduled to graduate this semester.

Since you have received a National Direct Student Loan, you are required to receive an Exit Interview prior to termination of your studies.

This interview is a review of the NDSL Act and includes a discussion of provisions for postponements, deferments, cancellations and repayment schedules; therefore, it is important that you attend.

For your convenience, we have scheduled three group meetings as follows:

Wednesday	April 29 at 3:00 p.m.	Room T 101
Thursday	April 30 at 2:00 p.m.	Room T 101
Thursday	April 30 at 7:00 p.m.	Room F 101

Please plan to attend one of these meetings, since your diploma will be held until the interview is complete.

Copy

E Barrett, Robert B.
COUNT NUMBER 40242

I. QUARTERLY PAYMENT PLAN

DUE DATE	UNPAID BAL. OF PRINCIPAL	INTEREST DUE	PRIN. AMOUNT DUE	TOTAL PAYMENT DUE
6/ 1/ 82	3000.00	22.50	75.00	97.50
9/ 1/ 82	2925.00	21.94	75.00	96.94
12/ 1/ 82	2850.00	21.38	75.00	96.38
3/ 1/ 83	2775.00	20.81	75.00	95.81
6/ 1/ 83	2700.00	20.25	75.00	95.25
9/ 1/ 83	2625.00	19.69	75.00	94.69
12/ 1/ 83	2550.00	19.13	75.00	94.13
3/ 1/ 84	2475.00	18.56	75.00	93.56
6/ 1/ 84	2400.00	18.00	75.00	93.00
9/ 1/ 84	2325.00	17.44	75.00	92.44
12/ 1/ 84	2250.00	16.88	75.00	91.88
3/ 1/ 85	2175.00	16.31	75.00	91.31
6/ 1/ 85	2100.00	15.75	75.00	90.75
9/ 1/ 85	2025.00	15.19	75.00	90.19
12/ 1/ 85	1950.00	14.63	75.00	89.63
3/ 1/ 86	1875.00	14.06	75.00	89.06
6/ 1/ 86	1800.00	13.50	75.00	88.50
9/ 1/ 86	1725.00	12.94	75.00	87.94
12/ 1/ 86	1650.00	12.38	75.00	87.38
3/ 1/ 87	1575.00	11.81	75.00	86.81
6/ 1/ 87	1500.00	11.25	75.00	86.25
9/ 1/ 87	1425.00	10.69	75.00	85.69
12/ 1/ 87	1350.00	10.13	75.00	85.13
3/ 1/ 88	1275.00	9.56	75.00	84.56
6/ 1/ 88	1200.00	9.00	75.00	84.00
9/ 1/ 88	1125.00	8.44	75.00	83.44
12/ 1/ 88	1050.00	7.88	75.00	82.88
3/ 1/ 89	975.00	7.31	75.00	82.31
6/ 1/ 89	900.00	6.75	75.00	81.75
9/ 1/ 89	825.00	6.19	75.00	81.19
12/ 1/ 89	750.00	5.63	75.00	80.63
3/ 1/ 90	675.00	5.06	75.00	80.06
6/ 1/ 90	600.00	4.50	75.00	79.50
9/ 1/ 90	525.00	3.94	75.00	78.94
12/ 1/ 90	450.00	3.38	75.00	78.38
3/ 1/ 91	375.00	2.81	75.00	77.81
6/ 1/ 91	300.00	2.25	75.00	77.25
9/ 1/ 91	225.00	1.69	75.00	76.69
12/ 1/ 91	150.00	1.13	75.00	76.13
3/ 1/ 92	75.00	0.56	75.00	75.56
		461.30	3000.00	3461.30

. MONTHLY PAYMENT PLAN = 29.00

I PREFER PLAN I ____ II____. SIGNATURE ________________________ DATE _____

Best Available Copy

REVIEW OF NATIONAL DIRECT STUDENT LOAN PROVISIONS

While a student at Ithaca College, you borrowed from the National Direct Student Loan Fund - a contributory program sponsored by this College and the Federal Government. Since you will begin to repay this loan in the near future, we would like to outline instructions for making payment, enumerate qualifications for deferment and/or cancellation of payments, remind you of your obligations, and explain to you your rights. We suggest you safeguard this review as you may wish to refer to it sometime in the future.

Enclosed is a statement and master card. They will be sent to you every time a payment is due and with special notices. The current status (total outstanding) of your loan(s) appears in the boxes on the left-hand portion of each statement. The amount due appears on the right side with principal and interest, current and delinquent, detailed separately. Return the master card with payment as it will expedite processing.

A. Repayment terms - your repayment schedule begins nine consecutive months after you cease to be at least a half-time student. These nine months are a grace period during which no interest accrues and no payment is due. Interest begins to accrue at the end of the grace period and your first payment will be due one month later if you opt for a monthly repayment plan or three months later if on a quarterly plan. Payments may be deferred or postponed if you qualify (refer to paragraphs B & C).

1. Monthly installments - 120 equal payments of principal and interest or $15, whichever is greater.
2. Quarterly installments - 40 equal payments of principal plus interest on outstanding balance or $45, whichever is greater.

Interest is computed at the rate of 3% per annum on the outstanding balance. Outstanding interest is deducted from all payments; remainder is applied to principal.

B. Deferment of Repayment - your repayment schedule may be interrupted interest free for:

1. Any period during which you are pursuing at least a half-time course of study at an institution of higher education.
2. A period not to exceed three years during which you are a member of:
   (a) U.S. Armed Forces
   (b) Peace Corps
   (c) VISTA

The deferment form is on the reverse side of your statement. This form must be filed annually as long as you claim such status.

C. Postponement of Repayment - when partial cancellation (refer to paragraph D) is predicated upon performance (i.e. teacher or military service), and when your repayment schedule calls for payments prior to the completion of the year of service, you are eligible for a postponement of payment until the end of the service year. The postponement form is also on the reverse side of your statement.

D. Cancellation of Repayment - your loan may be cancelled in part or in full if you qualify for one of the categories listed below:

	Type	Yearly Rate	Maximum Cancellable	Qualifications	Action to be Taken
1)	Teacher	10%	50%	a) Loan granted prior to 7/1/72.	a) At beginning of service year, complete reverse of statement form (postponement section)
				b) Full-time teacher	b) At end of service year file completed form "Request for Partial Cancellation"
				c) For a complete academic year	
				d) In a public or nonprofit elementary, secondary school, or college	
2)	Teacher	15%	100%	a-c) Same as Number one	a-b) Same as Number one
				d) In a public or nonprofit elementary or secondary school	

	Type	Yearly Rate	Maximum Cancellable	Qualifications	Action to be Taken
				e) In a school with a high concentration of students from low-income families (determined by U.S. Commissioner of Education), or for teaching handicapped children	
3)	Teacher	15-30%	100%	a) Loan granted after 7/1/72	a-b) Same as Number one
				b-e) Same as Number two	
4)	Teacher	15%	100%	a) Same as Number three	a-b) Same as Number one
				b-c) Same as Number one	
				d) In a head start program	
5)	Military	12½%	50%	a) Loan granted between 7/1/70 and 7/1/72	a-b) Same as Number one
				b) Completed one calendar year of active duty in the U.S. Armed Forces	
6)	Military	12½%	50%	a) Loan granted after 7/1/72	a-b) Same as Number one
				b) Completed one calendar year of service in an area of hostilities	
7)	Permanently Disabled	-	100%		a) Contact NDSL section, Ithaca College, for details
8)	Bankruptcy	-	100%		a) Same as Number six
9)	Death	-	100%		a) Same as Number six

Prior to the end of a year of cancellable service, a form will be sent which you must complete and have certified. Part of your loan will be cancelled upon return of this form providing you have not exceeded the cancellable limits. Care should be taken to insure that the cancellation form is returned promptly as delinquency is determined from the beginning, and not the end, of the postponement period.

E. Special Provisions and/or Conditions

1. You are permitted to accelerate repayment of your loan, in part or in full, at any time without penalty.
2. You are required to keep the National Direct Student Loan section informed of any change or changes of address.
3. You are responsible for all attorneys fees and other costs and charges necessary for collection of any amount not paid when due.
4. In the event you fail to meet a scheduled payment of any installment due on your note(s), the entire unpaid balance including interest due and accrued shall, at the option of Ithaca College, become immediately due and payable.
5. Should you not be able to meet a payment for any reason, please keep us informed as we may be able to help you and avoid unnecessary legal action.
6. In New York State, minority is not a defense for non-payment of loans granted for educational purposes.

We hope this is a complete review of all the provisions of your National Direct Student Loan. If it is not, or if you are still confused, please contact us. Send all inquiries to:

NDSL Section
Bursar's Office
Ithaca College
Ithaca, New York 14850

INFORMATION QUESTIONNAIRE

The following information is needed to up-date our records. Please complete this questionnaire.

1) Name: ______________________ I.D. #: ______________

2) Soc. Sec. #: ______________ Dvr. Lic.: State: ______________

Number: ______________

3) Home Bank: Name: ______________________

Address: ______________________

4) Credit Cards: Name: ______________ Number: ______________

______________ ______________

______________ ______________

5) Auto Insurance:

Carrier: ______________________ Policy Number: ______________

6) Relative who will always know your address:

Name: ______________________

Address: ______________________

7) Senior year room-mate: ______________________

8) Close College Friends: ______________________

9) Ithaca College professors with whom you are likely to keep in touch:

______________ ______________

10) Plans for the next two years: ______________________

____

____

Signature ______________________ Date ______________

ITHACA COLLEGE

LOAN STATEMENT

MAIL TO: BURSAR'S OFFICE • NDSL SECTION • ITHACA COLLEGE • ITHACA, N Y 14850 • PHONE 274 3132

DATE	ALL TRANSACTIONS RECEIVED TO THIS DATE HAVE BEEN APPLIED

PAYMENT(S) DUE	NDSL	OTHER	TOTAL
DELINQUENT PRINCIPAL			
DELINQUENT INTEREST			
CURRENT PRINCIPAL			
CURRENT INTEREST			
PAY THIS AMOUNT			

	PRINCIPAL BALANCE	INTEREST BALANCE	OUTSTANDING BALANCE
NDSL(S)			
OTHER LOAN(S)			
IF YOU WISH TO PAY YOUR LOAN(S) ENTIRELY PLEASE REMIT THIS AMOUNT			

MAKE CHECKS PAYABLE TO **ITHACA COLLEGE - NDSL FUND**

To ensure prompt and proper credit, return the enclosed remittance copy with payment

BORROWER'S COPY

UNITED COMPUCRED COLLECTIONS, INC.
P.O. BOX 11350 CINCINNATI, OHIO 45211

ITHACA COLLEGE - JDI08

United Compucred Collections Procedures

General: United Compucred Collections, Inc. will provide a five letter program consisting of an Express-Gram, demand letter and three third-party letters for the NDSL accounts.

Submission of Accounts: Copies of the Student Loan bill will be used to send accounts to United Compucred.
The UCC number from a blue collection form will be written above the student name and address.
Page two of the UCC form will be retained for updating the account.
All account assignments and other communications are to be directed to:

Mrs. Robin Keller
United Compucred Collections, Inc.
P. O. Box 11350
Cincinnati, OH 45211

Updating: Stops, suspends and resumes will be made by sending the appropriate stub from page two of the collection form.
Address corrections and other changes may be handled by memo addressed to Robin Keller. Always refer to the UCC claim number.

NOTE: Letters are run on Wednesday each week. All update information should be sent on Friday. Last minute changes may be reported by phone to Robin Keller at 1-800-543-1351.

Reports: Every two weeks a status report will be sent showing all accounts currently active and any activity since the last report.
This report should be retained as documentation of the College's collection efforts.
Suspended accounts will remain on the report until resumed or stopped.

UNITED COMPUCRED COLLECTIONS INC.
P.O. BOX 39485
2780 BANNING RD.
CINCINNATI, OHIO 45239
PHONE
(513) 931-2400

DEBTOR INFORMATION

☐ MR.
☐ MS.
☐ MRS.
CUSTOMER FILE NUMBER

NAME

ADDRESS

CITY STATE ZIP

TOTAL
AMOUNT OWED $

CHECK ONE-REASON
☐ ACCOUNT ☐ CHECK ☐ CONTRACT

REMARKS

M147184

MAIL IMMEDIATELY WHEN
PAYMENT IS MADE IN FULL

M147184

STOP

MAIL TO: UNITED COMPUCRED COLLECTIONS, INC
P O BOX 39485
2780 BANNING RD
CINCINNATI, OHIO 45239
PHONE
(513) 931-2400

MAIL TO RESUME SERVICE WHEN DEBTOR FAILS TO MEET ARRANGEMENTS PREVIOUSLY AGREED TO.

NEW BALANCE
$______

M147184

RESUME

MAIL TO: UNITED COMPUCRED COLLECTIONS INC
P O BOX 39485
2780 BANNING RD
CINCINNATI OHIO 45239
PHONE
(513) 931-2400

MAIL IMMEDIATELY WHEN ARRANGEMENTS FOR PAYMENT HAVE BEEN MADE.

M147184

SUSPEND

MAIL TO: UNITED COMPUCRED COLLECTIONS, INC
P O BOX 39485
2780 BANNING RD
CINCINNATI OHIO 45239
PHONE
(513) 931-2400

XPRESS-GRAM

MR. JACK DANAHY
49 WOODMAN CIRCLE
WEYMOUTH, MA 02190

NDSL ACCOUNT #01-8267

AMOUNT: $125.35

YOUR NDSL ACCOUNT WITH ITHACA COLLEGE IS IN DEFAULT.

THE PROMISSORY NOTE YOU EXECUTED GAVE THE COLLEGE THE RIGHT TO DEMAND IMMEDIATE PAYMENT OF THE ENTIRE PRINCIPAL BALANCE, ACCRUED INTEREST AND COLLECTION COSTS UPON DEFAULT OF ONE OR MORE SCHEDULED PAYMENTS.

YOUR CHECK, IN PAYMENT OF THE BALANCE INDICATED ABOVE, MUST BE RECEIVED WITHIN FIVE DAYS.

IF THERE IS A REASONABLE EXPLANATION FOR YOUR FAILURE TO MEET THIS DEADLINE, YOU MUST CONTACT THIS OFFICE TO AVOID FURTHER ACTION.

ITHACA COLLEGE
STUDENT LOAN OFFICE
ITHACA, NY 14853
607-274-3132

ITHACA COLLEGE
Ithaca, New York [illegible]

October 8, 1979

Mr. Jack Danahy
49 Woodman Circle
Weymouth, MA 02190

RE: NDSL Account #01-8267
AMOUNT: $125.35

Dear Mr. Danahy:

Your continued failure to make payment or contact us regarding your delinquent NDSL account is a serious matter.

You have been put on notice that, because of your default, the College has the right to require immediate payment of the entire principal balance, accrued interest and collection costs.

In accordance with directives from HEW, we hereby demand that you bring your account current within the next ten days.

If you do not comply with this final request, your account will be placed for collection.

Very truly yours,

Anne E. Hyland
Bursar
607-274-3132

AEH:rk

United Compucred Collections, Inc.

P O BOX 11350
CINCINNATI, OHIO 45211

October 22, 1979

Mr. Jack Danahy
49 Woodman Circle
Weymouth, MA 02190

CREDITOR: Ithaca College
Student Loan Office
Ithaca, NY 14853
Ms. Jean Hamil
Ph: 607-274-3132
AMOUNT OF DEBT: $125.35

Dear Mr. Danahy:

In compliance with Federal Law 95-109 (15 United States Code 1601 et. seq.), you are hereby put on notice that your delinquent account has been forwarded to us for collection by Ithaca College.

Immediate payment of your debt will forestall further disposition of this matter.

Unless you, within 30 days after receipt of this notice, dispute the validity of this debt, or any portion thereof, this debt will be assumed to be valid. If you, within 30 days after receipt of this notice, notify the undersigned in writing that the debt, or any portion thereof, is disputed, we will obtain verification of the debt or a copy of a judgment against you. Upon written request, we will provide you with the name and address of your original creditor, if different from the creditor listed above.

Send payment today. To ensure prompt credit, direct payment to the above named creditor; or send payment to us. Be sure to enclose this letter with your payment for proper identification.

Very truly yours,

W. L. Symmonds
President

WLS:rk

UNITED COMPUCRED COLLECTIONS, INC.
P. O. BOX [illegible]

November 5, 1979

Mr. Jack Danahy
49 Woodman Circle
Weymouth, MA 02190

CREDITOR: Ithaca College
Student Loan Office
Ithaca, NY 14853
Ms. Joan Hamil
Ph: 607-274-3132
AMOUNT OF DEBT: $125.35

Dear Mr. Danahy:

You are hereby notified that your failure to respond or pay your debt has been reported by us to Ithaca College.

It is imperative that you make full payment in 14 days, or contact your creditor at once. If 14 days pass without full satisfaction of this debt, they will be notified by us to pursue this matter by any lawful means at their disposal under state and federal law. You may avoid further action by sending your payment today. To ensure prompt credit, direct payment to the above named creditor; or send payment to us. Be sure to enclose this letter with your payment for proper identification.

Very truly yours,

A. B. Stineman
Vice President

ABS:rk

AKRON • ATLANTA • BOSTON • BUFFALO • CHARLESTON • CHICAGO • CINCINNATI • CLEVELAND
COLUMBUS • DALLAS • DETROIT • JACKSONVILLE • LEXINGTON • LOS ANGELES • LOUISVILLE
NEW YORK • PITTSBURGH • SAN FRANCISCO SPRINGFIELD • TAMPA • TOLEDO • WINSTON SALEM

United Compucred Collections, Inc.
P O BOX 11350
CINCINNATI, OHIO 45211

November 19, 1979

Mr. Jack Danahy
49 Woodman Circle
Weymouth, MA 02190

CREDITOR: Ithaca College
Student Loan Office
Ithaca, NY 14853
Ms. Jean Hamil
Ph: 607-274-3132
AMOUNT OF DEBT: $125.35

Dear Mr. Danahy:

According to reports from our collection mangement, their efforts have proved unsuccessful in soliciting your cooperation with Ithaca College.

Please he advised that I am notifying them as of this date that they may wish to contact their attorney concerning available remedies in compliance with federal and state law.

I feel sure you will agree that immediate arrangements for payment of this debt is the best solution. Send payment today. To ensure prompt credit, direct payment to the above named creditor; or send payment to us. Be sure to enclose this letter with your payment for proper identification.

Very truly yours,

W. L. Symmonds
President

WLS:rk

Mr. SIMON. Father Weiss, we are very pleased to have you here. My original written statement this morning said Reverend Weiss was going to be commenting on the regulations. I thought it was our colleague from New York here. I asked if someone had tried to make him a member of the clergy. But it turned out we have a Father Weiss here.

We are pleased to have you.

STATEMENT OF REV. ROBERT F. WEISS, PRESIDENT, ROCKHURST COLLEGE, KANSAS CITY, MO.

Reverend WEISS. I am pleased to be here.

I am Father Robert Weiss, President of Rockhurst College in Kansas City, Missouri.

Rockhurst is one of the 28 Jesuit colleges and universities in the United States. And I speak today on behalf of the Association of Independent Colleges and Universities, and also the Association of Jesuit Colleges and Universities. I am also serving as President of the Independent Colleges and Universities of Missouri.

In my written testimony I have given details of the status of repayment of the national student direct loan program nationally for the NICU institutions and also for Rockhurst.

I want to briefly note that our default rate at Rockhurst for the most recent year, 1980 to 1982, is 5.56 percent. We expect that that rate will be further reduced.

Just to give you an idea of the dimensions of our program, during that year we loaned $249,000, $188,000 came from collections of our own outstanding loans that were paid back by students, and only $66,000, because of the reductions in the program, came from additional Federal contributions.

Approximately 10 percent of our student aids, all student aids, exclusive of guaranteed student loans, come from the NDSL program. I am sure that the members of this subcommittee are well aware of the importance of this program in the total picture of student financial aid.

For myself I have always felt that student loans were an especially appropriate way to assist students in financing their education. I would like to single out just two reasons that I think are a particularly attractive way.

First, it enables the student to share in the cost of their education and to repay these loans for the use of others later on. I think that is a very good way of financing.

The second point is that it teaches the student early in life a sense of responsibility. It aquaints him or her with a method of financing that most Americans use to buy a house, buy a car, and which many businesses and our Government itself uses as a means of financing. Besides that, of course, the NDSL program really does help the poor students, those students who do not have access to the guaranteed student loans because of the problems of dealing with a banker, trying to get to those loans.

Unfortunately, as we all know, in the early days of NDSL there was a lack of clear understanding of the repayment obligation. The variety of forgiveness provisions, just simple unfamiliarity with the program, meant that really few institutions could do a good job of preparing students for this obligation and keeping the necessary records for the followup that would be needed to administer the program.

I remember myself having to persuade many students and their parents that this was a good, sound, honest way to finance their education. And I think in trying to sell people on the loan program, in many cases people were given the impression that, well, this might not necessarily have to be repaid. Now that is just—I do not think we did that at Rockhurst, certainly not deliberately, but there was a lot of confusion.

The elements of good collection Dr. Whalen has mentioned but I think they come down to three: the preloan interview. We stress with the student the obligatory nature of their payment, we make clear what is involved, and we obtain good background information on the student, his family, his grandparents, the addresses, job descriptions, so that we can trace the student.

Most of our loan defaults, especially the older ones, were due to losing track of the student. I think that is just a common problem. They move so often that we just have no way of contacting them.

Second then, we now keep close touch with the student, we insist on an exit interview when he leaves.

Third, we keep careful track of delinquencies and follow up on them.

Let me mention briefly, since it was in your letter, Mr. Chairman, that you were interested in the cost to the institution, in 1976–77 we had advanced the student loans $1.328 million, cumulatively. Besides the cost of running the financial aid office, the interviews in setting up loans for students, at that time we spent $1,157 for collection agencies and about $5,000 of staff time, so about $6,500 to collect loans.

In 1980–81, when our default rate got down to 5½ percent, about, our total lending was $2.344 million; our collection agency costs were $7,549, and we had a full-time staff person working on this at a salary of $14,916. So we spent about $24,000 in direct institutional costs in collecting loans; not in the process of giving loans and inverviewing, counseling students.

Mr. **Simon**. And what was that total again, $1.5 million?

Mr. **Weiss**. At that time our cumulative amount was $2.344 million.

I would like to suggest that these proposed regulations to penalize those with 20- to 25-percent default rates and to stop Federal contributions where the rate is over 25 percent, although it obviously would not affect us at Rockhurst, really ought to be reconsidered.

First of all, it is too late in this cycle of assigning aids to introduce this kind of change. That has been really one of the problems in making these kinds of things effective. They are put in hastily, and the institution has to scurry around to manage to do what they can to recoup themselves for next year. This is the time that we should be awarding funds, not still hearing about ways that they are going to be analyzed.

The second thing is that institutions and current students are being penalized by poor handling that either may have been corrected or took place a long time ago.

Third, if these regulations are simply a means to reduce the budget, then I think it ought to be said and they ought—we ought not to use this kind of means to simply reduce the funding.

As I suggested at the end of my written testimony which you have, there are at least two ways in which this default issue could be dealt with I think more fairly.

First would be to use the 1980–81 academic year as a base and give a 1-year phase in so institutions would really know what these regulations are going to be and they would have some opportunity to put in place good procedure for handling them.

Second, perhaps a better way, would be to revise the method of computing the default rate to base it on loans that were made or which come into the collection phase during a more recent period, say the last 5 years. This would encourage greater diligence and would recognize the progress that is made. Right now it is very difficult. You can turn these loans over to the Government but then you lose the possibility of further use of that money.

In conclusion, let me state that the NDSL and now the much larger guaranteed student loan program, really have made attendance at Rockhurst and the independent institutions all over the country possible for many students who simply would not have been otherwise able to attend.

Now the guaranteed student loan program is vastly larger and is extremely crucial for us. I was glad to hear Mr. Peyser bring out in the testimony that that program is operating well.

We have learned a lot and I think that we can operate this in a way that it is an effective way of helping students. On the other hand, NDSL does provide for that smaller number of students who really do not have effective access to guaranteed student loans.

I thank you, Mr. Chairman, for this opportunity and I certainly would welcome questions.

Mr. SIMON. Thank you very much.

[Prepared statement of Robert F. Weiss follows:]

PREPARED STATEMENT OF REV. ROBERT F. WEISS, PRESIDENT, ROCKHURST COLLEGE, KANSAS CITY, MO.

Mr. Chairman and Members of the Subcommittee, I am Father Robert F. Weiss. I am president of Rockhurst College, an independent liberal arts college in Missouri. I am here today on behalf of the National Association of Independent Colleges and Universities, which represents 870 colleges and universities, 42 state associations, and 28 special purpose organizations.

I am grateful for the opportunity to present testimony to the Subcommittee on the status of repayments in the National Direct Student Loan (NDSL) program, both at Rockhurst, and generally at all independent institutions. I would like to share with the Subcommittee some of NAICU's concerns with the new Administration proposal to penalize institutions with default rates deemed unacceptable by the Education Department (ED), and to relay to you the importance of this program to independent higher education.

For most of the history of this program, the Department of Health, Education, and Welfare did little to assist colleges in defining good lending practices or assisting in collection activities. Approximately five years ago, HEW issued regulations and guidelines to help colleges to reduce their default and delinquency rates.

In recent years, both individual colleges and universities and the Federal government have cooperated to reduce the rate of default in this program. But, on January 7 ED published a Notice of Proposed Rulemaking (NPRM) in the Federal Register proposing to reduce and/or eliminate the NDSL Federal Capital Contribution (FCC) for schools with certain default rates. Let me be clear that we are not here advocating high default rates or poor lending practices, but rather are suggesting less onerous means of assuring just the opposite while continuing this very important program.

The NDSL program was established under Title II of the National Defense Education Act of 1958 to provide loan funds at postsecondary educational institutions in order for them to make long-term, low-interest loans to qualified students who needed financial assistance to pursue a course of study on at least a half-time basis. The Federal share under the program is 90 percent -- the Federal Capital Contribution -- and the remaining 10 percent is supplied by the institutions. Institutions are responsible for making and collecting loans. This program marked the beginning of the Federal government's efforts to provide financial assistance to students who sought higher education. It was a deliberate response by the Federal government to a perceived need that a greater number of individuals should have access to higher education resulting in a more highly educated citizenry.

This Federal acknowledgement of the need for a Federal role in higher education has continued through the creation of six other student aid programs (Pell Grants, Supplemental Educational Opportunity Grants, College Work-Study, State Student Incentive Grants, Guaranteed Student Loans, and Parent Loans). These seven programs provide various forms of aid to a student through grants, work-study opportunities, and loans.

When the NDSL program began, obtaining a loan in order to finance one's education was not a common nor comfortable action by most individuals. Yet, over the course of time, students have taken a greater role in paying for their studies at an independent college or university. Within the independent sector of higher education, students rely on a combination of these three forms of aid, and any variation in one form has a direct effect on the other forms.

According to data compiled by the National Institute of Independent Colleges and Universities on undergraduate students who receive at least one form of aid, 37 percent received NDSLs in Academic Year (AY) 1979-80. The average NDSL award for these students was approximately $800 in AY 1978-79 and AY 1979-80. The following table depicts by income level for both AY 1978-79 and AY 1979-80 the average NDSL award, cost of attendance, percent of recipients receiving aid, and percent of the student aid package that comes from the NDSL award.

NDSL Awards for Dependent Undergraduate Students

	AY 1978-79				AY 1979-80			
Income by Thousands	Mean Dollar Amount Per Recipient	Cost of Education	Percent of Student Aid Budget	Percent of Recipients Receiving Aid	Mean Dollar Amount Per Recipient	Cost of Education	Percent of Student Aid Budget	Percent of Recipients Receiving Aid
$ 0-6	$804	$5,067	16%	36.8%	$811	$5,467	15%	34.7%
6-12	786	5,202	15	49.2	824	5,688	14	46.2
12-18	817	5,418	15	52.0	839	6,007	14	46.0
18-24	829	5,652	15	52.2	834	5,941	14	43.0
24-30	782	5,955	13	45.4	842	6,499	13	44.5
30-36	771	6,263	12	47.0	786	6,723	12	36.9
36 & Above	787	6,702	12	41.9	830	7,079	12	38.8
All Incomes	$803	$5,712	14%	48.9%	$801	$5,796	14%	43.0%

Source: The Initial Impact of the Middle Income Student Assistance Act Upon Undergraduate Student Aid Recipients at Independent Colleges and Universities, National Institute of Independent Colleges and Universities, June 1981.

The January 7 NPRM proposes to reduce the FCC for institutions with default rates greater than 10 percent and not more than 25 percent, and to eliminate any FCC to those institutions with default rates greater than 25 percent. An appeals process is provided for those institutions which may be able to show significant improvement in their default rates. In reviewing the Education Department's "orange book," which reports the default rates for all participating institutions, the following data was gathered regarding NAICU member institutions.

Comparison of NDSL Default Rates in Ay 1979-80
for All Institutions and NAICU Members

	All Institutions		NAICU Members	
Default Rate	Number	Percent	Number	Percent
10% and Below	1,482	45%	491	65%
Above 10% to 25%	983	30	212	28
25% and Above	799	25	51	7
Total	3,264	100%	754	100%

In order for the Subcommittee to understand how NDSL affects an individual institution, I would like to share with you Rockhurst College's experience with the program during the last five years. Rockhurst has participated in the NDSL program for over 20 years. Our total enrollment is 3,000 students (of which 1600 students are enrolled in the college's evening division or Master in Business Administration programs and do not receive NDSL awards). The majority of our students come from families with incomes below $25,000 causing them to seek assistance from the Federal government in order to help finance their education at an independent college. The total cost of education at Rockhurst College in 1981-82 is approximately $6,300. Nearly all of our students who receive NDSL loans are receiving some other form of aid (either gift assistance -- Pell Grants, SEOG, or the Missouri State Grant Program and self help programs -- work-study and loans).

NDSL Program at Rockhurst College

Academic Year	Average Loan	FCC	Collections - Number of Students	Amount Lent - Number of Students	Default Rate
AY 1977-78	$710	$138,729	$ 92,736 - 522	$231,778 - 326	12.0%
AY 1978-79	712	154,670	123,171 - 573	263,621 - 370	6.1
AY 1979-80	665	143,246	126,937 - 587	256,961 - 386	5.7
AY 1980-81	631	104,127	153,314 - 640	264,782 - 419	5.5
AY 1981-82	607	66,005	188,035 - 661	249,107 - 410	(est.2.0)

This table demonstrates how important the NDSL program is to the independent sector of higher education. Even within the last five years, the number of students seeking assistance from the NDSL program has increased and the average loan amount was decreased in order to respond to the reduced FCC amount while providing more Rockhurst students with some amount of needed NDSL loan capital. On average, in AY 1980-81 the NDSL award represents 10 percent of the student financial aid budget at Rockhurst College. Replacing any portion of these lost funds would be very difficult.

In addition, our default rate has steadily decreased from 12 percent in AY 1977-78 to 5.5 percent in AY 1980-81. We are pleased that the NDSL default rate has decreased in the last four years, and are continually working to reduce it even further. But this task has not been an easy one for either Rockhurst College or our students. At Rockhurst College, we have placed a great emphasis on pre-loan counseling sessions in order to inform student borrowers of their obligation to repay. We believe it is essential to discuss with our students their rights, obligations, terms of their loan, and allow the students to ask questions about this loan agreement. For most students, obtaining an NDSL loan is their first solo financial undertaking. Thus, we continue to place importance on the student/lender arrangement, and conduct exit interviews for those Rockhurst students leaving in order to advise them of their future financial obligation and rights.

The Education Department contends that the proposed regulation is necessary in order to more fairly distribute the FCC. We believe that it is important to ensure stability and accountability in the NDSL program, and that institutions should uphold their part of the NDSL agreement with the Federal government when making and collecting loans. But we do have some concerns with this NPRM.

This proposed regulation was published in the Federal Register on January 7 with comments due to ED by February 22. We understand that ED is planning to publish a final rule by mid-March. Currently ED is compiling the relevant data from institutional AY 1980-81 Fiscal-Operations Report and Application in order to calculate default rates. The rate of default in AY 1980-81 will be used to determine an institution's FCC for the coming academic year. This process is expected to be completed by mid-March (when ED will send institutions notices of tentative allocations for AY 1982-83). Thus, it appears that no matter when the final rule is published, institutions will suffer from the Education Department's tardiness and stringent guidelines. Spring is the time to tell students what they can expect, not the time to finally learn of the size of the Federal grant. Let me remind you that in AY 1979-80 the average NDSL award represented 14 percent of the financial aid package for a student attending an independent college or university.

A second concern of NAICU is the method of calculating the rate of default. It appears that some inequities may result for both institution and student. Some institutions have made few NDSL loans, yet have high default rates because these few loans were left in the default state. Thus, students who choose to attend that institution may not be able to utilize the NDSL program because of past actions dating back ten to fifteen years. It seems unfair to deny access to students now because of previous defaulters.

It is also important to note that even though some institutions have had default rates above 10 percent in the past -- ever since ED, in cooperation with colleges and universities, took more aggressive steps to reduce default rates -- those NAICU institutions with default rates above 10 percent have reduced their default rates, and many to default rates below 10 percent.

The most direct effect of this proposed regulation will be on those institutions with default rates greater than 25 percent, but colleges and universities with default rates greater than 10 percent and not more than 25 percent will suffer reductions and possible elimination of their FCC. ED has not yet completed an analysis of this proposed regulation to determine the amount of money that will be saved by reducing or eliminating some institutions' FCC, or the number of colleges and universities that will be most severely affected. NAICU believes it is important and essential for the viability of the NDSL program to reduce the default rates, but believes it is imperative to inform schools of the ramifications of this proposed regulation.

Independent colleges and universities have already suffered substantial reductions in NDSL funding.

NDSL Funding Levels for Fiscal Years 1977 - 1981

Fiscal Year	NDSL Appropriation	Independent Sector Allocation	Rockhurst College FCC
1977	$323.2 Million	$120.7 Million	$138,729
1978	325.7	122.8	154,670
1979	310.5	132.0	143,246
1980	286.0	116.6	104,127
1981	186.0	69.2	66,005

As NDSL funding decreased, so did, for the most part, the share of NDSL funds to the independent sector and to Rockhurst College in particular. The most drastic reduction occured when the NDSL appropriation was reduced from $286 million in FY80 to $186 million in FY81. In turn, Rockhurst College's FCC decreased by 37 percent during that time period. Although the number of borrowers increased from 640 to 661, the average loan decreased from $631 to $607. In fact, in almost every year, despite the level of FCC received by Rockhurst College, the number of students served by the NDSL program increased as total dollars decreased. Even with the changes in student aid packaging in recent years, the NDSL data from Rockhurst College demonstrates that more students are in need of NDSL loans to help finance their education at an independent college.

Therefore, we believe that while the proposed regulation is offered to penalize those institutions with default rates greater than 10 percent, its main purpose is to use the default rate issue as a means to cut the cost of the NDSL program this year. We understand that the NDSL program may even be abolished in the FY 1983 budget proposals. Thus, even if some schools receive reduced FCC allotments and the authorizing statute provides a means for excess funds to be reallocated, it seems highly unrealistic that this so-called excess FCC will ever be redistributed according to legislative formula. Every institution suffers, regardless of their default rate.

We believe that there are at least two possible ways of dealing with the default issue without putting undue burden on students and institutions and without having administrative actions used to reduce budget outlays.

One way would be to use the information on the AY 1980-81 Fiscal-Operations Report and Application as a base year. Institutions would then be on notice that if their default rates are not below 10 percent or 25 percent by the time they submit the 1981-82 Fiscal-Operations Report, their FCC would be reduced. That would allow a one-year phase-in of the procedure proposed in the January 7 NPRM.

A second approach would be to modify the method for computing the default rate of an institution. We suggest that only those loans that were made or came into collection within the last five to ten years be counted in the formula used to determine an institution's default rate. This is because some of the loans currently used in calculating institutional default rates may have been in default for 10 or 15 years during the earlier days of the program. This would allow some control on default rates by requiring institutions to exercise greater due diligence in making and servicing loans while not penalizing current students for old practices.

Mr. Chairman, I appreciate the opportunity to present these remarks and would be pleased to respond to your questions.

Mr. SIMON. Let me ask a general question of each of you.

First, what does it cost to go to Ithaca College and to Rockhurst College, assuming you are a resident student, not a commuter?

Mr. WHALEN. $8,000, that is room, board and tuition, and books.

Mr. WEISS. Our total cost is $6,300, including all the things allowed in figuring tuition. Our tuition is actually $3,380, so it is a somewhat lower cost institution than others.

Mr. SIMON. You say $6,300 and $8,000. How does a student; let's say you come from a family where you are eligible for every student program, how does a student put that together at your two institutions?

I come from a family with no income, $6,000 a year income and those families do exist in my district—how do we put that together at your college?

Mr. WHALEN. Well, we have a financial aid office and we have a financial aid officer who is well-trained in the use and the abuse of these programs.

I think the best way to answer that question for me is to say that we try to package a program of scholarships from Ithaca College, grants and loans, loans where we feel the student has some ability later on to pay. For example, the financial aid officer is somewhat sensitive to the fact that if a student is tremendously economically disadvantaged and perhaps educationally disadvantaged, and is taking on college maybe as the first member of that family, to saddle that student with a large loan program is to create a major problem. So we are sensitive to that.

Let me give you a couple of figures that may answer you a little more broadly.

At Ithaca College we have about 4,800 students. I wrote down a few figures here. At the present time we have 940 students of the 4,800 on Pell grants for approximately $950,000. We have 200 students on the SEOG program for $200,000. We have 1,300 students on Ithaca College scholarship money for $1.6 million. We have 250 students on campus employment and we have guaranteed student loans for 2,800 students of $7 million, which gives you some idea of the way in which we look at the student and how we package it.

I am not a financial aid officer expert.

Mr. **Simon**. No. What I am really trying to do is to put together a package, if I were a student; if I am not a national merit scholar, I may struggle to get a B and I have a family with limited income. What it appears to me we are moving toward is to make it extremely difficult for a family of limited means to go to your college and a heck of a lot of other colleges.

I was reading the Chronicle of Higher Education the other evening where they mentioned in Canada, of the foreign students, it used to be 30 percent were from the poorer nations, now it is down to 10 percent from the poorer nations.

My fear is—well, we are doing the same with foreign students in the United States, aside from our present problem, which is not in our national interest, it doesn't seem to me. But in a sense we are moving in that same direction with a developing nation within our own Nation. I am very much concerned. That is why your testimony here today is appreciated a great deal.

Mr. **Weiss**. Let me try to give you just a picture, a similar case at Rockhurst.

First of all, of the $6,500, we aim at trying to meet, if they have full need, of trying to meet 85 percent of the need. We are fortunate in Missouri in having the Missouri student grant program which of course incorporates the SSIG portion from the Federal Government.

But we would get $1,500 under that, we would give the maximum under the Pell grant, which has varied somewhat, but say that is $1,500, $1,600, we would give $800 under work study and then a national defense student loan of about $1,500.

Now if the student then—if that does not meet the need, we would try to give some Rockhurst money or guaranteed student loan money, but we would expect the student to achieve some of that, even though he is from a family that cannot give any aid themselves, the student would achieve some of that from work or other means.

But as you say, we are getting to the point though wherein if these programs are going to be further reduced, it will mean the poor student won't have the opportunity to go to even a moderatepriced institution like Rockhurst, which is less than the national average.

Mr. **Simon**. In effect, that not only deprives the student but it deprives your college of a mind and an economic mix that is important for the right kind of educational product?

Mr. **Weiss**. Exactly.

Mr. **Whalen**. You asked about—I can give you now an example of how we put a package together. Let's say we cost $8,200, this is an example. We would give $1,200 in college work study, $1,250 in NDSL. We do not give the maximum $1,500, we limit it to $1,250. The student might be expected to have $600 from summer employment, $1,250 in a Pell grant, $1,000 in SEOG.

New York State has the tuition assistance program which perhaps would give the student $1,800. This would be a student with great need. Still he has to come up with the $600 and $1,100; if that student were in great need and we were trying to keep him away from too much debt, we might package it that way.

Mr. **Simon**. But it is tough.

Mr. **Whalen**. It is extremely difficult to do and it is extremely difficult now because of the flux. We are trying to look at next year and plan the financial aid package for next year and it is almost an impossible situation at the moment because we really have rather poor information on what is going to happen, what we might be able to expect.

Mr. **Simon**. We cannot provide it right now.

Mr. **Whalen**. I know it is not your fault.

Mr. **Simon**. I was interested, Father Weiss, in your suggestion that we use the academic year 1980-81 fiscal year as another alternative. Something along that line appeals to me a great deal.

Mr. Erdahl?

Mr. **Erdahl**. Thank you very much, Mr. Chairman.

As you are aware, and I will inform our two witnesses, it may be somewhat difficult for me to be completley objective about this whole business of student loans because we have three sons at St. Olaf College, a very fine private college that you are both aware of, in Minnesota. Again, it is an expensive venture for our family.

A couple of things you have said seem so basic. We have had in the media and sometimes among our colleagues, criticism of the whole loan program. It seems so basic to do what you two have done.

First of all, do a good orientation job, good selection process, a good followup, basically I guess what every banker does in making loans. He is careful about who he is getting and he does a good job of collecting.

I wrote down here "keeping track of the students." Many of them are willing to pay but if they do not get notice, it is probably easier to pay the electric bill and other bills before they pay this one. That seems to be basic.

I would just underscore this has been good positive testimony we have received. I thank the two presidents for being with us. I think it does underscore that these programs and this assistance is absolutely essential if we are going to help some students get a shot at education today.

As a member of the minority on the committee, I must confess to a certain uneasiness with some of the programs that we have been asked to accept in the past because, as I think I mentioned to the committee yesterday, and some other witnesses, as we are under the gun to make these cuts, not only do we make economic judgment, we are also making a social judgment, as you said, Mr. Chairman, at a $6,500 or $7,000 income.

Without this assistance in a family, that means that son or daughter is not going to have a shot at a higher education. I do not think that we in this Congress want to be the instigators or, frankly, I will be blunt, supporters of a system that would do that.

I just thank you very much for what I think is very helpful testimony that we can utilize as we try to defend, maybe restore or at least maintain some very essential programs in this area.

Mr. SIMON. We thank you both for your contribution very much.

Mr. Weiss?

Mr. WEISS. Thank you very much.

Thank you, Mr. Chairman. I apologize for not having been here for the testimony. I have another subcommittee that I had to run over to for a few moments. So I won't ask any questions at this time.

I do want to express my appreciation to the witnesses. I have had a chance to just briefly scan the testimony. I will be reading it in great detail. I am sure this will be a continuing story unfolding for at least the balance of this year.

Thank you.

Mr. WHALEN. May I make one statement?

Mr. SIMON. Yes.

Mr. WHALEN. In response to what Mr. Erdahl said, over the last 20, 25 years the Federal Government and colleges and universities, the educational community have been in, it seems to me, a partnership. We built a financial aid structure that is multifaceted and fragile, complex, and if we are forced to cut, as we must and as we have, I think it is tremendously important that that relationship between the Government and the higher education community be maintained so that we can communicate some of the problems that will occur, as you pointed out, and how that impact might be lessened if we turn this dial up and this one down.

NDSL is important for many of our schools. GSL is important for many of our schools. I am terribly concerned about the fact that for so many years we were in partnership. I hope that that partnership does not break down. We probably need it more than we have before.

Reverend WEISS. May I add one word?

Mr. SIMON. Yes.

Reverend. WEISS. I really do believe that the GI bill was one of the best investments that this country ever made in terms of the return to the citizens of greater productivity and better education. Beginning with a NDSL program in the fifties, we have come a long way to satisfying the long-time American dream of access, which was mentioned earlier, and of giving students a choice. I think it will be a catastrophe of great dimension if we back off of that. It is something that we, unfortunately, will not be aware of next month or next year; it will be 10 years, 15, 20 years before we realize the seriousness.

That is one of the problems with these changes that are taking place. Because it is advanced funding on these programs, most of them, we do not notice the effects right away, but we are dealing with something that I think is terrific and I am sure all of the members of the subcommittee who are so friendly to this are also aware of the tremendous importance not only for our students and schools but for our country.

Mr. SIMON. Thank you both.

I may add, my concern is not only a quantitative one, but qualitative. We may be putting the squeeze on your schools and the students so that the net result is going to be great damage. The same Chronicle mentioned each of the last 5 years there have been three fewer volumes published for university libraries in this country. That is not something that erupts into headlines, but it is an erosion that I fear may become too typical of what is going to take place in our country if we are not very careful.

We thank you both very much.

We stand in recess until 2 p.m. We will at 2 p.m. have a joint hearing with the Subcommittee on Elementary and Secondary and Vocational Education on the social security reductions in student benefits.

[Whereupon, at 12:07 p.m., the subcommittee adjourned.]

[Material submitted for inclusion in the record follows:]

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OF COUNSEL

MARYLAND OFFICE

VIRGINIA OFFICE

March 9, 1982

Ms. Margaret Henry
Office of Student Financial Assistance
Room 4018, ROB 3
400 Maryland Avenue, S.W.
Washington, D.C. 20202

Re: NPRM Changes in Funding "Procedure" for NDSL, CWS, and SEOG; Fed. Reg. 1-7-82

Dear Ms. Henry:

This will serve to supplement the statement filed February 22, 1982, on behalf of our client, the Association of Independent Colleges and Schools ("AICS") in the above-captioned matter.

Attached is a copy of a form letter dated March 1978 to institutional presidents concerning the disposition of certain NDSL program notes. It appears as Appendix J at page 209 of the current "Audit Guide, Campus-Based SFA Programs, Office of the Inspector General, June 1980." The first sentence of the final paragraph on the first page states as follows:

> "Your institutional default rate will be calculated each year on the basis of the annual fiscal-operations report as of June 30."

We suggest that this letter supplements and reinforces the discussion in our statement of February 22, 1982, concerning the improper calculation of the default rate for NDSL as presently practiced. It particularly illustrates default rates being based on the annual fiscal-operations report, the instructions of which, if carried out as stated, utilize the "principal amount outstanding" rather than the "principal amount past due and in default" as the basis for the computation. We continue to maintain that this is improper and contrary to the regulations, as well as inconsistent with proper procedure in the semi-annual "Report of Defaulted Loans" in ED Form 574.

We hope this will be of assistance to you as you review the NPRM concerning NDSL default penalties.

Respectfully submitted,

THE ASSOCIATION OF INDEPENDENT
COLLEGES AND SCHOOLS

Through its General Counsel,

SACHS, GREENEBAUM & TAYLER

By:
Richard A. Fulton

RAF/csd

APPENDIX J

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
OFFICE OF EDUCATION
BUREAU OF STUDENT FINANCIAL ASSISTANCE
WASHINGTON, D.C. 20202

March 1978

Dear President:

The purpose of this letter is to transmit instructions for the disposition of certain National Direct Student Loan Program notes which have been classified as uncollectible, and to point out the characteristics of the notes which may be assigned to the United States. Any note which your institution assigns to the United States is assigned without recompense. In other words, your institution forfeits its interest in any note assigned to the United States.

All NDSL notes which are classified as uncollectible must be valid instruments; that is, they must contain proper signatures, and correct entries to amounts advanced and dates. For some institutions audits and program reviews may have already identified defective or invalid notes for correction. However, should such invalid instruments exist today, the institution which owns the notes must buy them by depositing into the Fund an amount equal to the uncollected principal. It may then proceed to attempt collection as if the transaction originally involved institutional funds only.

Due diligence in attempting to obtain collections must be demonstrated. Subpart C of the NDSL regulations covers "Loan Collection - Due Diligence." Since this standard was published in 1976, you are not required to show full compliance with it for efforts made in prior years. However, reasonable efforts along the lines of this standard and Appendix 17 of the NDSL manual must be demonstrated to the satisfaction of the Office of Education.

An important objective should be the conservation of capital in your Student Loan Fund. Collection studies have shown that second attempts to collect on long overdue notes are frequently successful. Therefore, any delinquent note, no matter when the repayment period began, on which the slightest chance of recovery of funds still exists, should be retained by the institution and its collection actively pursued. Defaulted notes which are included in your report as of one June 30 would not be shown as defaulted in the following June 30th report if the note has been retained and the borrower has been brought back into repayment status.

Your institutional default rate will be calculated each year on the basis of the annual fiscal-operations report as of June 30. Notes which have been assigned to and accepted by the United States will be included in the basic default rate thereafter. On the other hand, notes which have been assigned to and accepted by the United States will be subtracted from your basic default rate to obtain an adjusted default rate. This adjusted default rate will be used as the basis for determining the effectiveness of your operation of this phase of your program in comparison with other institutions.

If you determine that you have valid NDSL notes on which due diligence has been performed, and there appears to be practically no chance of collection on these notes, you may then assign them to the United States without recompense.

An original OE Form 553, Assignment of Defaulted Note(s) must be completed for each loan which you wish to assign to the United States, and be certified by an institutional official who has the authority to relinquish the institution's interest in the note. A sample of this form is enclosed, and additional copies should be requested in writing from:

Mrs. Florence V. Taylor
Chief, Services and Collections Section
Campus and State Grants Branch, DPO
Bureau of Student Financial Assistance
U.S. Office of Education
Washington, D.C. 20202

A copy of the Procedural Guidelines and General Information statement is also enclosed.

Questions pertaining to this matter may be directed to Mrs. Taylor on telephone number 202-245-9727.

Sincerely yours,

Carolyn Betts

Carolyn Betts
Director
Division of Program Operations

Enclosures

THE CALIFORNIA STATE UNIVERSITY

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WASHINGTON OFFICE

February 4, 1982

FEB 5 1982

The Honorable Paul Simon
U.S. House of Representatives
227 Cannon House Office Building
Washington, D.C. 20515

Dear Congressman Simon:

On behalf of the California State University, I wish to respond to the discussion in your hearing yesterday on the GAO report, "Students Receiving Federal Aid Are Not Making Satisfactory Academic Progress: Tougher Standards are Needed" and to submit the enclosure for the record. The California State University is the largest system of four-year undergraduate and graduate (masters degree level) education in the United States. However, not one of our 19 campuses was included in the GAO sampling. We also have well-defined standards of academic progress in relation to eligibility for student aid. Satisfactory progress is defined in terms of number of completed units at passing grades. Pages 46 and 48 of the enclosure from our Manual of Financial Aid Policies and Procedures specifies factors which must be included and excluded in the determination of completed units.

The failure to include colleges and universities such as those in our system supports the criticism launched at the GAO. Unfortunately, the press has published its articles summarizing the report. Since reporters seldom rewrite their stories, the damage has already been done. However, we are thankful for your action to publicly correct the record.

Sincerely yours,

Judith Wortman

Judith S. Wortman
Director, Federal Relations

B. SATISFACTORY PROGRESS AND GOOD STANDING

1. **Federal Definition.** Federal student aid regulations specify that "satisfactory progress" and "good standing" are determined in accordance with institutional standards and practices and that scholastic probation should not disqualify a student for financial aid if, according to the standards and practices of the campus, he is maintaining satisfactory progress in the course of study he is pursuing.

2. **CSUC Definition** (for the purposes of determining financial aid eligibility).

   a. **Full-Time Undergraduate Student.** Completion of an average 12 units per quarter or semester attended during a *12-month period.* (Reference: Recommendation 1-j. Trustees Internal Audit Report No. 73-3).

   b. **Half-Time Undergraduate Student.** Completion of a minimum average of 6 units per term during an *academic year.*

   c. **Full-Time Graduate Student.** Completion of an average of 8 graduate level units per term during a *12-month period.*

   d. **Half-Time Graduate Student.** Completion of a minimum average of 4 graduate level units per term per *academic year.*

   e. **Exceptions.** On a case by case basis, an exception to the above unit completion requirements may be made upon receipt of written recommendation from the Counseling Center, student's faculty advisor, or Financial Aid Advisory Committee as determined by local campus policy. Documentation must be retained in student's folder. If a student is recipient of an EOP grant, see Section 603-E-3-c.

3. **Inclusion in Terms of Award.** When "satisfactory progress" or "good standing" are included in conditions for receipt and retention of award, recipient must be given an explicit statement of such terms when award is made (SA 73-26).

C. ACADEMIC UNIT LOAD VERIFICATION

1. **Prior to the First Disbursement.** Verification of enrollment in "the required" number of units must be made prior to the first disbursement.

2. **Prior to Each Additional Disbursement.** Verification of enrollment on at least a half-time basis shall be made prior to each additional disbursement within a term.

3. **Census Date.** Confirmation of enrollment in "the required" number of units must be made for all aid recipients from census date until load roster print-out *as soon as available.*

NOTE: If a student receives an EOP grant, see Section 603-E-3 for unit enrollment and unit completion requirements.

D. UNIT DROPS

1. **Prior to the Census Date.** Executive Order No. 171 permits withdrawal from courses(s), without restriction or penalty, during a period established by the campus, which must be no later than the census date. If aid is disbursed prior to census date, any unit drops not cleared through the Financial Aid Office will be identified in the required review of the census date unit load roster (see Section 306-D-2).

2. **After Census Date.** A system for automatic referral of students to Financial Aid Office (or prompt notification of unit drops) must be developed between Financial Aid Office

and appropriate campus office(s). The Financial Aid Office shall take appropriate and timely follow-up action including reduction, cancellation, and/or recovery of award if recipient is no longer carrying required number of units (SA 73-26).

a. If student has been awarded Work-Study funds, recovery of any earnings determined to be in excess of a revised financial aid eligibility shall *not* be requested unless the student misrepresented his or her factual circumstances, upon which the eligibility for financial aid had been determined.

b. If Work-Study is reduced or cancelled, the employer should receive written notification.

E. WITHDRAWALS

1. **Notification of Withdrawals.** A system for prompt notification of withdrawal by aid recipients must be established between Financial Aid Office and appropriate campus office(s).

2. **Refund of Financial Aid.** The Affidavit of Educational Purpose, signed by all recipients of federal funds (SA 74-54), specifies that such funds will be used solely for expenses related to attendance at the campus.

   a. **Amount of Refund.** Whether and to what extent a student shall be required to refund his aid depends upon length of time student has been attending classes during the term and the judgement of the appropriate reviewing official(s) as to the portion of the award required for school-related expenses for that time. Basis for decision must be fully documented. If required refund involves Work-Study funds already earned, see Section 306-D-2-a and b.

   b. **Due Diligence in Collection Efforts.** If student cannot be interviewed regarding repayment of funds (i.e., student discontinued class attendance without officially withdrawing, or withdrew by mail), due diligence must be evidenced in campus efforts to collect any required repayment as follows:

      (1) Send letter to the student explaining financial obligations resulting from withdrawal and stating that a hold has been placed on student's records until such obligations have been cleared. (References: SA 73-26 and Sections 42380 and 42381 of Title 5 of the California Administrative Code).

      (2) If student does not respond, send a second letter (identical to the first) by certified mail, return receipt requested.

   c. **Delay of Loan Repayment.** If loan was awarded during term student withdrew, repayment can be made in accordance with provisions of student's promissory note (i.e., immediate repayment of loan is not required unless in judgement of the Financial Aid Office or the Business Office or both, immediate repayment should be required). Student should receive exit interview documents including the repayment schedule.

3. Effect of Withdrawal on Completion of Required Number of Units

   a. Do not consider units attempted and subsequently cancelled by authorized withdrawal in determining completion of required average number of units.

b. If a student has received a Financial Aid Warning Letter (see Section 306-F-3) specifying a deadline for completion of units from a previous term, the deadline shall not be affected by such withdrawal unless unusual circumstances (documented) warrant special consideration.

DETERMINATION OF COMPLIANCE WITH SATISFACTORY PROGRESS REQUIREMENT

1. **Checking Units Completed.** At the end of each academic term, official records of units completed by all financial aid recipients must be checked promptly upon receipt of such records by the Financial Aid Office to confirm that the "required" number of units has been completed (SA 73-26).

2. **Interpretation of Grades** (for the purpose of determining financial aid eligibility).

   a. Following shall be considered as units completed:

      (1) "A" through "D" grades.

      (2) "CR" (Credit)

   b. Following shall *not* be considered as units completed:

      (1) "F" grades.

      (2) "NC" (No Credit).

      (3) "W" (Withdrawal).

      (4) "AU" (Audit).

      (5) "U" (Unauthorized Incomplete).

   c. Following shall *temporarily* be considered as units completed, with final determination as noted (Reference: Executive Order No. 171):

      (1) "RD" (Report Delayed). Registrar will replace with a grade as soon as possible.

      (2) "SP" (Satisfactory Progress). To be replaced with appropriate final grade within one calendar year of date of first enrollment.

      (3) "I" (Incomplete). To be made up within one calendar year immediately following the end of the term in which it was assigned.

3. **Notification to Student.** The following procedures shall be followed:

   a. At the end of each academic term, if a student failed to complete at least a half-time unit load, or was disqualified, a "hold" shall be placed on the next disbursement and the student referred to the Financial Aid Office.

   b. Each term, at the first disbursement, all financial aid recipients shall be provided with a copy of a general policy statement regarding satisfactory progress. This statement shall remind the student of the "Agreement" signed at the time of accepting the offer, and of the required number of units which must be completed to maintain financial aid eligibility. This statement should also include a warning that subsequent financial aid may be denied if that number of units is not completed within the academic year.

EXCEPTION: This statement need not be distributed if the Financial Aid Office sends individual warning letters to all students who have not completed the "required" number of units at the end of each term. Such warning letter must include 1) the "required" number of units which were not completed in the preceding term, 2) the required number of units which must be completed to maintain financial aid eligibility (see Section 306-B-2), 3) the deadline for completing the deficit "required" units (see Section 306-F-4), and 4) the consequences, including probable denial of subsequent financial aid, if the required number of units is not completed during the specified time period. (Reference: Recommendation 1-j, Trustees Internal Audit Report No. 73-3.)

c. At the end of each academic year, the Financial Aid Office shall notify all aid recipients with unit deficiencies of the number of "required" units which were not completed, and whether or not financial aid for the subsequent year is being denied or continued on a probationary basis.

4. **Schedule for Completion of Required Number of Units.** The following schedule is predicated on the student's completion of an adequate number of units *up to* the time of the Financial Aid Warning Letter.

	Unit Deficiencies at End of Term	Terms During Which Units Must be Completed
Semester	Fall	Spring and Summer
	Spring	Summer and Fall
Quarter	Fall	Winter, Spring and Summer
	Winter	Spring, Summer and Fall
	Spring	Summer, Fall and Winter

5. **Excessive Unit Deficiency.** If the unit deficiency at the end of any term is so great that there is little probability that student would be able to make up the deficiency in required period of time, student must be advised regarding probability of discontinuation of aid in following term.

6. ***Termination of Financial Aid.*** *If it is determined, after review, that the conditions* specified in the warning letter (see Section 306-F-3 and 4) have not been satisfied, the student must receive a written notification of termination of financial aid eligibility.

307. CONFIDENTIALITY OF ALL STUDENT INFORMATION

"All documents, correspondence, and conversations between and among the aid applicant, his family, and financial aid officers are confidential and entitled to the protection ordinarily arising from a counseling relationship." (See Section 101-I.)

A. APPLICABLE LAW

Since Section 22504.5 of the California Education Code was repealed, the controlling law is now the 1974 Family Educational Rights and Privacy Act, sometimes referred to as the "Buckley Amendment". (See SA 75-87; 20 U.S.C. 1232g and 45 C.F.R. 99.)

In pertinent part, Section 99.31(a) (4) of the Federal regulations provides that:

> "(a) An educational agency or institution may disclose personally identifiable information from the education records of a student without the written consent of the parent of the student or the eligible student if the disclosure is --

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OVERSIGHT ON CURRENT STATUS AND ADMINISTRATION OF FEDERAL STUDENT ASSISTANCE PROGRAMS

THURSDAY, FEBRUARY 4, 1982

House of Representatives,
Subcommittee on Postsecondary Education,
Committee on Education and Labor,
Washington, D.C.

The subcommittee met, pursuant to call, at 10 a.m., in room 2261, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Weiss, and Erdahl.

Staff present: Marilyn McAdam, majority legislative assistant, and John E. Dean, minority senior legislative associate.

Mr. Simon. The subcommittee will resume its hearings.

This is another in a series we are holding on the student assistance programs. It is appropriate that we conclude this particular series with a representative of the Student Loan Marketing Association, better known as Sallie Mae, Mr. Edward Fox.

Sallie Mae serves as the secondary market for loans under the guaranteed student loan [GSL] program. This morning we will specifically be hearing about the current status of the programs operated by Sallie Mae as well as progress reports on loan consolidation, warehousing, and servicing of loans and implementation of the new authorities granted Sallie Mae in the 1980 amendments and the Omnibus Budget Reconciliation Act of 1981.

The role of Sallie Mae has become increasingly important as the GSL program has mushroomed in volume. Since its inception in 1973, Sallie Mae has invested over $4 billion in student loans. In the wake of anticipated changes in the GSL program, it is essential that Sallie Mae be available to provide financial and operational support to lending and educational institutions, State agencies, and parents and students participating in the student loan program.

We will also be hearing from other witnesses who will be telling us about the status of student financial aid programs and their importance to specific minority students. This knowledge is particularly important to us as we are about to receive the administration's budget requests.

Mr. Fox, we will start off with you. You may proceed as you wish.

STATEMENT OF EDWARD FOX, PRESIDENT, STUDENT LOAN MARKETING ASSOCIATION [SALLIE MAE]

Mr. Fox. I would like to thank you on behalf of our board and our chairman for the invitation to appear before your committee. We have given you a lengthy amount of material. I think it answered most of the questions that were requested of us, so I won't go over all of that and repeat it.

There are three points I would like to mention at the outset. Then I will take your questions.

First, in the 1980 amendments to the Higher Education Act we were permitted and were encouraged by this committee and by those amendments to provide a program of loans to States in support of their lending to students; itself as a primary or secondary market. That language was reasonably explicit. The comments in the report were explicit. But the Department of Education has taken the tack that there are some missing links in the legislation. If entities were to borrow from us, even though we finance ourselves on a fully taxable basis, looking at other legislation which was approved at that same time which would require that States that borrow only receive a half special interest allowance on the assumption they were coordinating the arbitrage profits associated with profits made from the sale of revenue bonds; in essence States have been told they cannot borrow from us.

We are very pleased that the leadership of the House and Senate has communicated with the Secretary, that that was not the intent of the law, that those who borrowed from us who were States should get the benefit of the full special allowance, and the States having difficulty marketing their bonds should have a secondary source of funds.

I refer you to my statement which talks about that in some detail. Hopefully, in order to give service to the States, which was not an issue, which was supported bipartisanly in the House and Senate a year and a half ago, it appears we are going to need some legislative tightening in order to provide that accommodation to the States. So we look to you for that help, sir.

Second, as you know, we are now selling our debt in the private capital markets which was the intent of the 1980 and 1981 legislation. An issue surfaced in which it appeared that entities which owed money to the Federal Government could only sell debt that was subservient to the Federal debt. That was not the intent of the original law. There were technical amendments approved in 1981 with the support of the House and Senate. That language has an expiration date of September of this year. I believe it was the intent of the Congress to review that, since it had come up on very short notice and to hopefully extend that so we would be able to finance ourselves. That, too, is an issue that has been dealt with at length in the material that I have given to you.

Finally, one authority that was given to us in the summer of 1981 as sort of a safety net, would permit us to make accommodations or to finance programs that were created with loans that were not insured by the Federal Government. For example, if there were a need in a geographic area or a class of students were not eligible for aid under an existing program, Sallie Mae would have the authority to put in place financing for accommodations that might be made by a school to a student or by a bank to a student that wasn't covered by Federal insurance or State insurance or reinsurance.

This has not been something that we expected to occur relatively quickly. As long as the existing programs, the GSIP, NDSL, and other programs were functioning and students hadn't been disenfranchised, we didn't expect these alternative programs would be created or made available to students. So we have made no provision to make such loans at this time. But it is a safety net program; so if students are disenfranchised, there would be other opportunities for Sallie Mae to participate in such loan programs.

All of a sudden we have started getting requests for information as to how such a program might work, particularly educational institutions are reviewing the financial situation of their students and finding that many already qualified for student loan programs which are not Government or State supported. They are wondering if they can make loans directly on an insured basis or induce banks to make loans to students to fill that void. Those institutions are also coming to us and looking for credit in support of those programs.

I would look to this committee for some guidance, because we have a limited amount of resources. There are a number of different programs to which we can provide credit or support. The issue is, really, What does the committee think about the possibility that certain groups who may have been disenfranchised, as you set qualifying standards for your programs, seek other forms of credit. And, since we have the statutory right to offer some kind of credit in support of those students, what do you feel about the possibility that we may indeed be called, or may have to finance, or have to consider financing that kind of request?

What comes down in the next few months may create an even larger pool of students who are not eligible for guaranteed student loans or NDSL loans, and I have no doubt they will be looking for any source of credit they can find. That, to some extent, means us. Any guidance you can give us about these uninsured loan programs would be appreciated.

That is my statement, Mr. Chairman.

[The prepared statement of Edward Fox follows:]

PREPARED STATEMENT OF EDWARD A. FOX, PRESIDENT AND CHIEF EXECUTIVE OFFICER, STUDENT LOAN MARKETING ASSOCIATION [SALLIE MAE]

The Student Loan Marketing Association (Sallie Mae) is a private, for-profit corporation chartered by Congress to provide a national secondary market for insured student loans made by private or state lenders under the federally-sponsored Guaranteed Student Loan Program (GSLP) and Health Education Assistance Loan Program (HEAL).

By congressional intent, Sallie Mae is structured along traditional corporate lines, with total responsibilities in the hands of a board of directors and a management team. The President of the United States appoints one-third of the 21-member board and designates the chairman from among the full membership. By statute, financial and educational institutions are permitted to own shares of voting stock of the corporation and each group elects one-third of the board of directors.

Sallie Mae provides a broad spectrum of private and state lenders -- commercial banks, thrift institutions, credit unions, state agencies and other primary lenders -- with a source of liquidity. It offers such lenders the opportunity to sell student loans at cash value or to borrow additional funds to support their student lending activity by pledging existing loans as collateral, thus serving as a secondary market for student loans.

In 1980, amendments to the basic enabling legislation, the Higher Education Act of 1965, enlarged Sallie Mae's statutory program and financing authority. Specific provisions authorize the corporation to consolidate or refinance student loans, to lend funds directly to state agencies where there is a certified shortage of loan capital, and to serve as a direct lender in states where there is a severe student loan shortage. Various amendments were included in the Omnibus Budget Reconciliation Act of 1981 broadening Sallie Mae's authorities as a prospective "safety net" in support of student credit. These include the right to purchase student loan revenue bonds and, with the approval of the Secretary of Education, to be an insurer under certain specific and limited conditions. A detailed discussion of these amendments can be found in the Appendix to this testimony.

In over eight years of operation, Sallie Mae has provided nearly $7 billion of support to lenders under the GSLP. As of December 31, 1981, its investment of $4.8 billion in the GSLP was equal to approximately 25 percent of all insured student loans outstanding.

Sallie Mae has worked with 1,200 lenders providing direct or indirect financial assistance to 2.0 million students in 51 states and territories. They include commercial banks, savings banks, thrift institutions, credit unions, educational institutions, states, agencies and state secondary markets. It has assisted in financing statewide programs in 14 states and the District of Columbia.

Sallie Mae obtains funds for its operations primarily from the sale of its debt obligations. In recent years it has financed its activities principally through the issuance to the Federal Financing Bank (FFB) of debt obligations guaranteed by the Secretary of Education. As announced by Secretary Regan on May 7, 1981, Sallie Mae has begun borrowing in the public markets without the guarantee of the federal government.

The corporation is expected to meet the same profit and loss standards, including a return on stockholders' equity, as a business without a government link. It pays full federal income taxes and has received no federal appropriations during its entire history. Sallie Mae is severing its ties with the federal government in connection with its funding activities. Its objective is to achieve its primary social purpose of expanding credit in support of access to postsecondary education by operating as a business organization subject to the disciplines and opportunities of the marketplace. As such, Sallie Mae considers itself to be a prototype for transforming a quasi-government organization into a private sector corporation that functions efficiently and profitably while fulfilling its original public service purpose.

During 1981, Sallie Mae provided $2.5 billion of secondary market support for the GSLP, a dramatic increase over the $1.4 billion in 1980. During the year the corporation's holdings of student loan related assets increased by 86 percent over 1980. From December 31, 1977, through December 31, 1981, the corporation has grown approximately ten-fold from $500 million to over $5.1 billion. Sallie Mae purchased $1 billion of guaranteed student loans in 1981, representing over 1400 transactions from institutions in almost every state in the union. During 1982, Sallie Mae expects to increase moderately its dollar volume of loan purchases against the 1981 performance. Warehousing advances (loans) totalled $1.4 billion in 1981, a dramatic increase over the $811 million made available in 1980. This growth was caused by lessened liquidity in the banking system and high interest rates which, in combination, create a cyclical demand for loans from Sallie Mae. Lowered interest rates and the previous utilization of available collateral by lending institutions suggests that demand for this service from Sallie Mae will diminish substantially in 1982. Over $500 million of lending in the Warehousing Advance Program in 1981 was against collateral other than student loans. This authority, first contained in the 1980 amendments to the Higher Education Act, permitted Sallie Mae to finance institutions that had not previously participated in the GSLP and permitted others that were lenders-of-last-resort to borrow from Sallie Mae to assure access to eligible students. Additionally, Sallie Mae provided $800 million of commitments to 58 institutions in 1981 to either purchase loans or lend at a future point in time. As of year end, such commitments, which are contingent liabilities of the corporation, totalled nearly $1 billion.

Sallie Mae was given the responsibility in the 1980 amendments to put in place a Loan Consolidation Program for certain qualifying students relative to the National Direct Student Loan Program (NDSL) and the GSLP. Approval from the Department of Education was not forthcoming until late in 1981, resulting in a pilot program first being offered during the fourth quarter. Because of the lack of a usable data base to identify prospective candidates for loan consolidation, and due to an extremely time consuming and costly process of origination, results of our pilot program are just beginning to become available. A very preliminary response from high indebtedness graduates suggests a relatively modest interest in the loan consolidation opportunity. However, Sallie Mae is committed to providing loan consolidation to all qualified students and anticipates closing $100 million of such loans during 1982.

Another program provided to Sallie Mae in the 1980 amendments clarified Sallie Mae's ability to lend directly to states. The Department of Education has taken the position that states borrowing from Sallie Mae on a direct basis would qualify for only a half special interest allowance. Many states have approached Sallie Mae during these difficult times in the student loan revenue bond markets, seeking financing from Sallie Mae. The interpretation given to Sallie Mae's authority, however, has prevented Sallie Mae from providing this assistance. Resolution of this issue is a critical necessity for the viability of programs in many state lending agencies. We are gratified that the majority and minority leadership of the House and the Senate communicated with the Secretary of Education that the Department's position was inconsistent with the intent of the original statute. If there is to be a viable Loans to States Program, the Congress is going to have to amend the statute, and we leave that to your judgment.

Various questions have arisen as to the purpose of amendments to the Sallie Mae provisions in the Omnibus Budget Reconciliation Act of 1981, and the activities of Sallie Mae since enactment of these provisions. These amendments were designed such that if, as some feared, the Act's changes to the GSLP resulted in a reduction in lender participation, other alternatives would be available for student credit. In fact, the Conferees specifically intended that with regard to certain provisions "the authority given Sallie Mae is only stand-by authority". H.R.Rep.No.208, 97th Cong. 1st sess. 743(1981). Sallie Mae has not yet exercised any of the new authorities provided in the Act. In addition, two of the Sallie Mae amendments were designed to correct deficiencies in the language enacted in the Education Amendments of 1980 relative to Sallie Mae's financing in the private capital markets. You should be aware that recently a small number of institutions have identified groups of middle income students who are no longer eligible for the GSLP and have approached Sallie Mae for discussions relative to a secondary market for uninsured student loans. Given the possibility that the eligibility of graduate students and others may again be reduced, Sallie Mae will be seeking your guidance as to its appropriate role in supporting student financing through non-federal loan programs.

We are appreciative of the support of the Congress in providing a technical amendment to Sallie Mae's enabling statute in 1981 which provided that "[t]he priority established in favor of the United States by section 3466 of the Revised Statutes (31 U.S.C 191) shall not establish a priority over the indebtedness of the Association issued or incurred on or before September 30, 1982". This amendment has created a temporary waiver as it is limited to debt issued or incurred prior to September 30, 1982. If this limitation is not removed before that date, Sallie Mae will find itself unable to finance its activities, to fund outstanding commitments, and to fulfill its congressional mandate of providing liquidity to the student loan market.

The most significant single development in the financial area during 1981 was the negotiation of an agreement with Administration officials in March that set the basic course of Sallie Mae's funding activities in the future. In exchange for an additional $2 billion of long-term financing authority at the FFB (bringing the total of such borrowing authority to $5 billion) the corporation agreed to accelerate the time schedule for re-entry into the capital markets to fund its activities. Specifically, the agreement called for Sallie Mae to end its borrowing from the FFB by September 30, 1982, or at the time a total of $5 billion of such borrowings was outstanding. Sallie Mae also agreed to enter the capital markets without the use of the full faith and credit guarantee of the Department of Education which was originally available until October 1, 1984. Working in concert with the Treasury Department, this agreement provides a sound base for Sallie Mae to begin financing its program acquisitions without federal support, as intended by Congress.

Sallie Mae began its reintroduction to the public capital markets in May, 1981, by issuing short-term discount notes. The notes have been well received by investors, often trading at lower yields than those offered by other agencies. Through December 31, 1981, more than $4.4 billion of discount notes were sold and $420 million were outstanding at that date.

The corporation is currently in the second stage of developing alternative financing instruments. A three-year floating-rate security, indexed to the 91-day U.S. Treasury bill, has been designed and has recently been sold at public offering at a relatively attractive rate by an investment banking syndicate. This instrument has been structured to protect SLMA from certain risks, as the index for the interest rate and the timing of the change of interest rate are virtually the same as those of the corporation's program assets. In addition, a task force has been established to evaluate the feasibility of issuing a security in the form of a student loan pass-through or participation certificate. Also, renewed efforts were begun late in the year to assess the opportunities for an equity issue.

Sallie Mae will rely heavily on the public markets to fund its operations in 1982, as only $400 million of additional FFB borrowing was available at the end of 1981 and has since been taken down. The primary source of financing, if available, will be floating-rate debt issued in quarterly public offerings of approximately $200 million. The corporation intends to rely on this relatively long-term, variable-rate debt, rather than on short-term discount notes, in spite of the somewhat higher costs anticipated from this strategy. It is important to maintain a conservative approach to managing Sallie Mae's affairs, given the corporation's high debt-to-equity ratio. Doing so will enable Sallie Mae to continue accessing the debt markets, and possibly the equity market over time as a result of a more stable earnings flow and a balanced balance sheet.

It is also possible that Sallie Mae will enter the Eurocredit markets in 1982 with a modest sized $50 to $100 million issue of floating-rate debt to introduce the corporation's name to that potentially valuable source of liquidity. Although such an issue is unlikely to be indexed to U.S. Treasury bills, it is expected that being prepared for proper market execution will enable the corporation to tap this market at a propitious time and at a reasonable cost. Preliminary planning for this financing is already underway.

Under its enabling legislation, Sallie Mae is subject to federal income taxes as a private, for-profit corporation.

Taxes on its 1981 income, both current and deferred, were $14.9 million. Since inception, Sallie Mae has incurred total tax liability of $42 million. After provision for taxes, 1981 corporate earnings were $18.0 million. Dividends of $1.5 million, or less than eight percent of earnings, were paid to stockholders that are financial and educational institutions eligible to participate in the GSLP. The remainder was retained by the corporation and invested in further support of student loans.

Servicing continues to be the most serious problem for Sallie Mae and other major holders of guaranteed student loans. During 1981, Sallie Mae increased from 5 to 10 the number of contract servicers acting as agent to collect its loans and actively entered the servicing business itself. By December 31, 1981, Sallie Mae was collecting on over $100 million of student loans, or approximately 6 percent of the $2 billion of student loans owned. The corporation is in the process of developing its own software system at considerable expense and hopes to have that system available and functioning by mid-1982, enhancing its collection capability and efficiency. Student loan servicing continues to be plagued by a lack of commonality among the requirements of the various guarantors which results in a plethora of differing routines in the collection system for each state. Hopefully, some method will be developed for encouraging uniformity where differences are not truly warranted. Other problems related to cost are brought about by frequent legislative change. For example, recent statutory changes have created 7 percent and 9 percent loans, and the possibility of 8, 12, and 14 percent loans. This increases accounting and data processing costs. Other changes having to do with deferment, grace period, minimum repayment, eligibility, and the rounding or lack of rounding of the special allowance to the nearest higher eighth of a percent, have required the separation of loans for different treatment and, in some cases, even the separation of the loans of a single borrower. This further complicates the system and increases costs. For a large holder of student loans, a combination of circumstances relative to an individual student can require some enormously complex solutions. The process is additionally impaired by the rigidity with which regulations are interpreted, often differing in each of the ten federal regions. I would hope that the Congress takes note of the operational aspects of any proposed changes in the GSLP so that the intent of the change can be managed within the framework of the existing banking system. We would be pleased to discuss specific operating problems with which we are familiar for legislative review as you have requested, but would hope that other means might be found. For example, if, under proper controls, the Secretary of Education was given limited authority to modify certain of the express terms and conditions of the program if a cost/benefit analysis indicates savings to the government and participants, positive changes could be made without resort to specific legislation. Hopefully, user groups such as state agencies, banks, educational institutions, student groups, and secondary market makers could help in advising the Secretary.

Changes in the banking and financial services industry could have an impact on the GSLP. We anticipate continued movement towards interstate banking and a continuance of interstate and interindustry mergers. This trend is accompanied by continued interest in planning for Electronic Funds Transfers systems, debit cards and other financial services which will require a considerable amount of data processing support. We are not convinced that the financial industry is willing to commit large dollar amounts or to give first priority for changes and development of student loan systems. Additionally, we are concerned about the banking systems' willingness to commit the dollars to the primary market in guaranteed student loans in the amount that current OMB and Department of Education loan volume projections for the next five years imply. We are also aware of the banking system's lack of interest in the parent loan program, primarily because of the high costs associated with immediate collection, the impact on other lending, and the probability of change.

Another concern has to do with the deteriorated condition of the municipal bond market. The major participants as buyers have been commercial banks and insurance companies during the last twenty years. Commercial banks have significantly reduced their appetite for municipal bonds as other forms of tax-reducing transactions, such as leasing, have become available to them. Casualty insurance companies as a group are no longer making a profit and so do not have income to shelter through the purchase of tax-free securities. That puts the burden on individuals and, since the 1981 tax legislation has reduced the maximum tax rate on unearned income from 70 percent to 50 percent, tax-free securities are less attractive. The result is a significant increase in the cost of marketing municipal bonds and, quite specifically, the cost of issuing student loan revenue bonds. Within the last thirty days one major state paid about 13 percent, all costs included, for a ten-year bond issue. To the extent that the market does not improve, many states who provide primary and secondary market services in support of the GSLP will have difficulty in continuing to provide service to eligible students and institutions.

Sallie Mae will also be faced with considerably higher costs of funds in 1982, financing itself in private capital markets without the full faith and credit of the United States. There is also a question as to the amount of funds which will be available to Sallie Mae in the marketplace. Systems development and control costs and servicing fees as discussed earlier will also add to Sallie Mae's expenses. The reduced availability of funds, the high cost and higher operating expenses will, in all probability, result in a changing role for Sallie Mae proportionate to the GSLP.

The cost of funds to financial intermediaries, state agencies, and Sallie Mae is a function of the marketplace and will have to be managed in a sophisticated and, hopefully, in a successful manner by each institution. But, the costs associated with regulation and system development and collection can be improved through simplification of the program brought about by the desire of the Administration and the Congress to move in that direction.

Sallie Mae was established by an Act of Congress to meet a public service goal as a fully privately financed for-profit corporation. During its first eight years it has developed itself as a corporation with earnings and a balance sheet capable of supporting its social purpose with dollars that come, not from the federal Treasury, but from the private capital markets. Sallie Mae's development indicates that the private sector can, with some nurturing, create a vehicle to perform social services.

AMENDMENTS TO SALLIE MAE PROVISIONS OF THE HIGHER EDUCATION ACT ENACTED IN THE OMNIBUS BUDGET RECONCILIATION ACT OF 1981

Various questions have arisen as to the purpose of amendments to the Sallie Mae provisions in the Omnibus Budget Reconciliation Act of 1981, the Postsecondary Student Assistance Amendment of 1981 (the Act), Pub.L.No. 97-35, Section 538 (d) and the activities of Sallie Mae since enactment of these provisions. This memorandum will discuss each amendment, its purpose and the current activities or planned activities of Sallie Mae in implementing each provision.

The overall purpose of the amendments regarding Sallie Mae was to put in place a "safety net" for the Guaranteed Student Loan Program (GSLP). These amendments were designed such that if, as some feared, the Act's changes to the GSLP resulted in a reduction in lender participation, other alternatives would be available for student credit. In fact the Conferees specifically intended that with regard to certain provisions "the authority given Sallie Mae is only stand-by authority" H.R.Rep.No.208, 97th Cong. 1st sess. 743(1981). Sallie Mae has not yet exercised any of the new authorities enacted in the Act. In addition, two of the Sallie Mae amendments were designed to correct deficiencies in the language enacted in the Education Amendments of 1980, Pub.L.No.92-318, relative to Sallie Mae's financing in the private capital markets. Each of the amendments will be discussed in the order they appear in the Sallie Mae enabling statute, Section 439 of the Higher Education Act of 1965, as amended.

AUTHORITY TO DEAL IN NON-GUARANTEED OR NON-INSURED STUDENT LOANS

In a time of reduced federal support for postsecondary education, it was considered possible that individual institutions might be willing or feel compelled to invest capital to create non-federal loan programs for student credit. These loan programs would not qualify for any federal subsidies. The Act allows Sallie Mae to support such private efforts by acting as a secondary market for such non-insured loans as it does for the GSLP.

Sallie Mae has never envisioned that the level of non-insured loans available to students would be very large, given the continued existence of the GSLP. Aside from broad inquiries from educational institutions relative to loans to students ineligible for the GSLP, Sallie Mae has not been approached for a warehousing advance or the purchase of a portfolio of non-insured loans, Sallie Mae's normal secondary market activities. Sallie Mae is not a primary lender under any circumstance other than for purposes of the loan consolidation program.

LIMITED AUTHORITY TO PROVIDE A PROGRAM OF LOAN INSURANCE

This amendment was designed such that if, and only if, eligible borrowers are seeking and unable to obtain loans, and no state or nonprofit private institution or organization is capable of or willing to provide a program of loan insurance, the Secretary could enter into an agreement with Sallie Mae to provide such a program. This provides the Secretary and only the Secretary with the flexibility to allow Sallie Mae to become a loan insurer in the event of some isolated shortfall in student credit either in a state where no state agency exists or if a state agency becomes unable to carry out its function. Sallie Mae was also authorized to become a loan insurer for the purposes of the loan consolidation program. The Conferees stated their belief "that this stand-by authority is necessary to assure that loans are available to all eligible borrowers, regardless of geographical location. Under no circumstances is this amendment to diminish the strengths and viability of new or existing state guarantee or nonprofit agencies." H.Rep.No.208, 97th Cong.1st sess. 743 (1981).

Obviously, Sallie Mae has no unilateral authority under this provision. Any program of loan insurance must be carried out pursuant to an agreement with the Secretary. Neither Sallie Mae nor the Secretary has requested such an agreement and none exists. In fact due to the clear indication that such authority was given only as stand-by authority, Sallie Mae has not requested an agreement to become an insurer for the loan consolidation program but, instead, has agreed with the Department of Education that the Department will insure loan consolidation paper.

AUTHORITY TO DEAL IN OBLIGATIONS ISSUED BY STATE AGENCIES OR ELIGIBLE LENDERS

More than twenty states have become dependent on the sale of student loan revenue bonds to support the GSLP in their states. This authority provides Sallie Mae with the ability to purchase such bonds, thus providing an additional pool of assets to support revenue bond financing for student loans. This amendment to Section 439(d) in no way affects Sallie Mae's own financing authorities which are clearly defined and limited under Section 439(h).

Pending the resolution of several complicated tax questions, Sallie Mae has not bought, sold, held, underwritten or otherwise dealt with any such obligations. The only activity which Sallie Mae currently undertakes with regard to student loan revenue bonds is to provide underlying commitments to purchase the student loans made with the proceeds of the bonds. The same service is provided by other private financial intermediaries.

AUTHORITY FOR THE BOARD OF DIRECTORS OF SALLIE MAE

This amendment allows the Board flexibility in authorizing activities for Sallie Mae if the activities are "in furtherance of the programs of insured student loans...or will otherwise support the credit needs of students." Sallie Mae's corporate existence is defined by Section 439 of the Higher Education Act. Whereas most corporations have a charter with a corresponding provision, Sallie Mae's charter is Section 439. This authority is enjoyed by several other federally chartered corporations reflecting Congress' determination that such organizations' charters should be broadly defined, leaving determination of corporate activities to their governing boards.

This authority does not exist in a vacuum. Sallie Mae's Board, including public members and a Chairman appointed by the President of the United States, has the full fiduciary responsibility of any board of directors. The authority is limited by its own terms that any activities authorized must be in furtherance of student credit. Such activities that the Board could authorize would be subject to review by the Departments of Education and the Treasury as well as by Congressional oversight as provided in the statute. This flexibility allows Sallie Mae to respond to a changing credit environment for postsecondary education with new services or programs without the necessity of Congressional action but with accountability.

STATE TAX STATUS OF SALLIE MAE OBLIGATIONS

Since inception, Sallie Mae itself was exempt from state and local taxes other than property tax. This amendment clarified that Sallie Mae's bonds would be accorded the same treatment consistent with the law relative to other quasi-governmental corporations (TVA, Federal Home Loan Banks, Federal Home Loan Mortgage Corporation, Postal Service, Farm Credit Banks, etc.). This amendment does not affect the federal tax status of either Sallie Mae or its bonds, both of which are fully taxable under federal law.

GOVERNMENT PRIORITY IN BANKRUPTCY

This amendment was designed to provide that the government as a holder of Sallie Mae's debt instruments would in the event of bankruptcy stand equal with all other creditors. Due to Sallie Mae's extensive borrowings from the Federal Financing Bank, the existence of a federal priority effectively prohibits borrowing in the public capital markets, the intent of the Education Amendments of 1980. The amendment was inadequate to perform its purpose and a temporary solution was provided in the Older American Act Amendments of 1981, Pub.L.No.97-115 Section 18 (1981). This temporary solution is effective only until September 30, 1982, and should be made permanent prior to that time in order to allow public borrowing by Sallie Mae.

STUDENT LOAN MARKETING ASSOCIATION [SALLIE MAE]—A STATEMENT OF ITS PURPOSE, FUNCTION, AND OPERATING PROGRESS, FEBRUARY 1982

Established by the 1972 Amendments to the Higher Education Act of 1965, the Student Loan Marketing Association (Sallie Mae) is a federally chartered, privately owned corporation.

> "The Congress hereby declares that it is the purpose of this section to establish a private corporation which will be financed by private capital and which will serve as a secondary market and warehousing facility for student loans ... and which will provide liquidity for student loan investments." (20 U.S.C. Sec. 1087-2 (a))

Shareholder owned and controlled, Sallie Mae was established to support the federal government's Guaranteed Student Loan Program (GSLP). The GSLP is a program of federal insurance or reinsurance for loans obtained by students from state or private sources. Under this program, students obtain credit primarily from private lenders with the government providing insurance against defaults as well as interest subsidies to the borrower and to the lender.

In 1976, the Health Professions Education Act established a program of federally insured loans to graduate health professions students, the Health Education Assistance Loan Program (HEAL). The first HEAL loans were made in 1978. Sallie Mae is also authorized to provide a secondary market for loans made under this program.

Congress created Sallie Mae in a manner similar to many other quasi-government corporations. The purpose in establishing a secondary market was to enhance the attractiveness of student loans to banks and other primary lenders, thereby generating more private capital for the student loan market. Sallie Mae was intended to provide lenders with a source of liquidity -- a national, accessible secondary market where lenders could sell their student loans or borrow (warehouse) on the collateral of those loans. Program users were expected to provide the equity capital for the corporation and additional funds were to be obtained through the sale of government guaranteed debt obligations. The corporation was to use these funds to purchase or warehouse student loans. In this way, Sallie Mae would support the Congressional objective of maximizing private capital participation in student loan financing, consistent with the assurance of equitable levels of loan access by borrowers. In meeting its responsibilities, Sallie Mae is subject to review not only by its Board of Directors, but also by the federal government and the Congress. This pattern of oversight requires Sallie Mae to balance its public and private interests to assure corporate financial objectives as well as program objectives in support of the GSLP. In addition to statutory oversight and review, Sallie Mae, in the conduct of its business, must abide by regulations applicable to all holders of GSLP loans including those of the Secretary of Education and the state and private guarantee agencies.

Sallie Mae's status as a federally chartered, private corporation reflects two fundamental and complementary realizations by the Congress: first, that the public interest requires a viable and equitable system of student credit which will operate more effectively with the support of a national secondary market; and second, that a secondary market motivated by private sector objectives represents the least expensive and most efficient means of providing this support.

While Sallie Mae has neither requested nor received any appropriated funds, Congress did enable the corporation to borrow, through 1984, with the full faith and credit of the United States supporting its debt. In 1973 and 1974, Sallie Mae raised $400 million in the private debt markets as a new, untested corporation. From the establishment of the FFB in 1974 through 1980, Sallie Mae has borrowed exclusively from this source. The Bank lent to Sallie Mae at a rate higher than it paid for its funds, thus generating a profit for the FFB. Congressional intent behind the Bank was that those entities utilizing the full faith and credit of the United States should use the FFB in the interest of a more coordinated and cost efficient approach to financing.

In early 1981, Sallie Mae reached an agreement with the U. S. Treasury Department to limit its borrowing from the FFB and reenter the capital markets without use of the full faith and credit guarantee, by statute still available through September, 1984. Under this agreement, the corporation was eligible to borrow up to $5 billion on a long-term variable-rate basis through September, 1982. This debt extension program was completed in January, 1982. An additional result was the establishment of a Discount Note Program in May, 1981. During 1981, the Discount Note Program marketed by three major New York securities dealers emphasized short-term maturities and had an average outstanding balance of approximately $275 million.

In the last week of January, 1982, Sallie Mae began its next major phase of funding in the capital markets by issuing a three-year floating rate note, publicly issued in the capital markets by a federal agency. This method of financing is the foundation for future Sallie Mae debt since its interest expense will vary in a similar manner to Sallie Mae's assets. While the first issue of this new security was a success, it is important to note the substantially higher cost of this source of funds.

By statute, Sallie Mae's voting common stock can only be owned by eligible financial and educational institutions, and the majority of its directors are elected by those shareholders. Congress created Sallie Mae in a manner similar to several other corporations in that the constituency, for whom the corporation was established, was expected to provide the underlying capital. Sallie Mae raised $25 million in the private equity markets in 1974 and as of December 31, 1981, total stockholder equity, including retained earnings, was approximately $68 million. Effective January 1, 1981, the corporation's Board of Directors may also authorize the issuance of non-voting common stock to the general public.

The President of the United States appoints one-third of the twenty-one member Board of Directors and designates the Chairman from among the membership of the full Board. Sallie Mae's enabling legislation provided for the involvement in the corporation's financing activities of the Department of Education (only with regard to Sallie Mae's guaranteed debt financing) and the Department of Treasury. In addition, the Treasury Department is required by statute to provide the President of the United States and the Congress with a report on Sallie Mae's operations. Sallie Mae also is required to transmit to the President and Congress an annual report of its activities and operations.

In recognition of the Congressional intent that it exercise direction and control of the corporation, the Board of Sallie Mae has, from its inception, provided an active stewardship over the corporation. This is in keeping with the determination of Congress to structure Sallie Mae along traditional corporate lines, with total responsibilities in the hands of a Board of Directors and a management team.

Sallie Mae's enabling legislation requires the corporation to balance its public and private interests to assure that corporate financial and program objectives are in support of the GSLP. Sallie Mae, as a private, for-profit corporation, is not expected to assume risks which would have a materially adverse effect on the corporation's ability to operate as a viable secondary market. Identifiable risks to the corporation come from regulations, operations, and financial and economic fluctuations. Sallie Mae also is a public purpose institution chartered by the government to support national goals in the area of student credit. As such, Sallie Mae is expected to play a leadership role, within the bounds of sound financial practice, in encouraging and supporting lenders in the continuation of GSLP lending activity and by setting standards which are widely acknowledged as supporting sound loan origination and administration.

An examination of Sallie Mae's program activities under its Loan Sale, Warehousing Advance and Commitment Programs reveals the extent of the corporation's support of the GSLP and the national objectives set forth by the Congress. Under its enabling legislation, Sallie Mae is authorized, pursuant to commitments or otherwise, to make advances on the security of, purchase or repurchase, service, sell or resell, offer participations or pooled interests, or otherwise deal in federally insured student loans or student loans that are insured by state or private guarantors participating in the GSLP. In 1981 Sallie

Mae was authorized to provide similar secondary market services for non-insured student loans. The corporation is prohibited from dealing with institutions that discriminate on the basis of race, sex, color, creed or national origin and from dealing with any commerical bank with deposits in excess of $75 million, which requires a customer relationship with the student or his or her family as a condition to receiving a student loan.

Under its Loan Sale Program, Sallie Mae offers to purchase loans made under the GSL and HEAL Programs. The Loan Sale Program provides funds to lenders and, because the corporation utilizes a network of third-party servicing agents, relieves those lenders of the administrative considerations relative to loan servicing. Through its warehousing Advance Program, Sallie Mae provides liquidity to lenders against the collateral of their existing student loan portfolios or other U.S. Government issued or guaranteed obligations. By statute, institutions with advances collateralized by insured student loans must either reinvest all advance proceeds into additional guaranteed student loans or maintain a specified student loan portfolio level throughout the term of the advance. Institutions offering other collateral must fully reinvest all advance proceeds. Sallie Mae also provides the assurance of future funds through the issuance of forward commitments. These commitments, for both the Loan Sale and Warehousing Advance Programs, have enabled many state and private lenders to maintain lending arrangements through the assurance of continued student loan credit.

The provisions of the Education Amendments of 1980 and the Postsecondary Student Assistance Amendments of 1981 provide a major challenge to the corporation. In addition to broadening the corporation's flexibility in meeting liquidity needs as a secondary market, Sallie Mae was also authorized to be active in the student credit market on a limited, direct basis. Specific provisions authorize the corporation to consolidate and refinance student loans, lend funds directly to state agencies where there is a certified shortage of loan capital, to serve as a direct lender or guarantor in states where there is a severe student loan shortage, to provide secondary market support for non-insured student loans, to purchase and underwrite student loan revenue bonds, and to provide such additional services as determined by its Board of Directors to be supportive of the credit needs of students.

Since inception, Sallie Mae has made available nearly $7 billion of support to lenders under the GSLP through its Warehousing, Loan Sale, and Commitment Programs. As of December 31, 1981, Sallie Mae's investment of $4.8 billion in the GSLP was equal to approximately 25% of all student loans outstanding.

In more than eight years of operation, Sallie Mae has worked with nearly 1,200 lenders in 51 states and territories. These institutions include commercial banks, thrift institutions, credit unions, educational institutions, state agencies and state secondary markets. Statewide programs are financed with assistance from Sallie Mae for the states of Colorado, Michigan, Minnesota, South Carolina, Kentucky, Kansas, Virginia, Mississippi, Oklahoma, and West Virginia.

Sallie Mae routinely does business with institutions of all types and sizes. These institutions include money center and regional banks as well as community oriented banks and thrift institutions and state agencies.

In terms of its business practices, Sallie Mae differentiates between high-risk lenders and high-risk student loans. Sallie Mae does not purchase loans unless they have been originated and maintained in compliance with appropriate statutory and regulatory requirements. However, the corporation does work with those institutions that are not in compliance to improve their understanding of these program requirements and generally has been able to complete transactions with most of them. Sallie Mae believes that it has the responsibility to purchase portfolios of loans from lenders whose origination practices are satisfactory, even though some of these institutions may have shown relatively high incidences of default. As such, Sallie Mae's portfolio contains an above-average number of loans made by open-access lending institutions. Many institutions have indicated that they would not support the GSLP without Sallie Mae standing by as a secondary market outlet for the loans they originate.

Not all primary lenders are willing or need to utilize the secondary market. For many financial institutions, the yields on these loans as well as other institutional factors encourage retention of student loans. However, knowledge of the existence of an accessible secondary market provides confidence to these lenders should they wish to utilize Sallie Mae.

Sallie Mae recognizes that as a secondary market, it has an important role in encouraging the primary market to lend to students in a nondiscriminatory and equitable manner. This understanding pervades Sallie Mae programs which reflect statutory requirements designed to encourage institutions to deal fairly with student borrowers. It is also reflected in the terms of the programs themselves, which attempt to balance the interests of lenders and the needs of Sallie Mae in a reasonable fashion. Sallie Mae also is deeply involved in assisting several states in their efforts to encourage student lending activities through the development of a direct lending capacity or in the establishment of effective state student loan guarantee programs. In addition, Sallie Mae actively promotes the use of its secondary market services to the financial community in the belief that the assurance of its support and participation will encourage the flow of private capital into the GSLP.

Sallie Mae is, under its Charter, a private corporation, governed by a Board of Directors in part elected by shareholders and in part appointed by the President. Sallie Mae's primary public goal is to improve access to student loan credit for eligible students and their parents who wish to finance a postsecondary education through the Guaranteed Student Loan or the Health Education Assistance Loan Programs. The corporation's position as a government-chartered enterprise implies a responsibility to encourage public interest objective consistent with sound financial practices expected of a private business. The pursuit of these goals, under its Charter, is fully consistent with the intent of Congress and reflects a balanced approach on the part of Sallie Mae with regard to meeting its public and private goals in support of the GSLP.

February, 1982

SLMA STATEMENT OF FINANCIAL POSITION
December 31, 1981
(Millions)

Assets	
Student Loans Purchased	$2,071.5
Warehousing Advances	2,754.9
Cash and Short-term Investments	168.2
Other Assets	176.7
Total Assets	$5,171.3
Liabilities and Equity	
Notes and Interest Payable	$5,095.4
Other Liabilities	8.2
Total Liabilities	5,103.6
Stockholders' Equity	67.7
Total Liabilities and Equity	$5,171.3
Committments Outstanding	929.5

Mr. SIMON. You asked for our guidance. Let me ask for your guidance. What is your feeling about what should be done on the uninsured loan situation?

Mr. FOX. It appears there is a large number of middle-income-students, students from middle-income families who are going to find it increasingly difficult to get credit, particularly as the eligibility standards are tightened. I think a properly managed program, where perhaps the banking industry takes a leadership role and the schools participate, and where the credit risk is shared by all parties, probably could deliver a reasonable amount of credit in support of those students' needs.

From a business point of view, I think a modest-sized program could be put in place, and it could be done in a way that would not be harmful to schools, banks, students, or ourselves.

I think the question really is the priority. Whether that group really has a priority as opposed to any other groups, or whether the pool of resources should be shared. I don't think that is a judgment that I, as a noneducator, or somebody who doesn't allocate resources in education, should really make.

Mr. SIMON. I guess one of my concerns is that we don't—you talk about shared responsibility here—that we both retain access in theory, but we retain access practically, also, so that our system doesn't get so complicated. People just don't understand how we proceed.

I note the presence of the president of Wittenburg University in the audience. How we maintain a program so that a student can go to Wittenburg University—the student counselor in high school may not have or doesn't understand NDSL, and all the things we talk about. I guess that would be one of my concerns.

Let me just ask you, you have had a chance, Mr. Fox, to take a look at the whole situation. If you were restructuring, as we now are—this isn't going to happen, but let's just say if you were restructuring the whole student assistance program—Sallie Mae doesn't exist, nothing exists—how would you proceed? That is a rather sweeping question, I realize, but you have had some reflection in this whole area of what we are doing and where we are going.

Mr. FOX. I think the first thing is to get a fairly good estimate of the resources that can be brought to bear by the Federal Government and the States in support of education. Then get a good census of those eligible for aid, and then make some judgment as to how you wish to distribute it in the least costly and most efficient way that you can. Today we have not only a very, very large number of programs, but we have a complexity to those programs and a constant change which builds incredible cost. It is ultimately borne by the consumer, which in this case is the student.

I am not sure what the distribution mechanism should be, whether it should be some central authority. One of the big problems I see in education is that the funds that are appropriated, whether it be for campus-based programs or student aid programs, is subject to change, reprioritizing, and schools never know from year to year what the totality of dollars going to education is going to be. So it is a very frustrating process for educators to try to get some kind of feel of what that flow of dollars is going to be.

In addition, things like the endowment funds are subject to fluctuation, reserving dollars that they count on, particularly those that come from Federal sources. It must be a hell of a thing to try to be a planner if you are in higher education, with the sources and uses of your funds subject to such gigantic change.

I would opt for simplification. I would look for a very simple kind of program, and I would look for some long-term commitment, no matter what the dollar amount is, so that during the planning process one could know in advance what level of dollars are going to be in the stream for some period of time.

You bring a student on this year and you have no idea what the aid package might be for the next 3 years for that student's academic career. It is a heck of a thing to try to plan. But some simplification, consistency, some sense of long-term funding so people have an understanding of what is coming and how to manage it. But clearly, simplification of the plethora of programs and reduction of the number would be the starting point.

A single loan program, a single grant program would clearly be, I think, in everybody's interest—well documented, reasonably thought through, not overly regulated. I'm not suggesting it shouldn't be controlled, but saying that the regulatory process has been a killer over the years as well.

Mr. SIMON. I tend to agree with you.

Does minority counsel have any questions?

Mr. DEAN. I have a couple of questions.

In your statement, you state that Sallie Mae is a private for profit corporation. The question has been asked me a number of times what benefits will Sallie Mae continue to receive after its Federal Financing Bank borrowing authority is terminated. In terms of the advantages that Sallie Mae will have for having had access to those funds, advantages Sallie Mae has over other private sector entities?

Mr. FOX. Well, as you know, we had access to $5 million from the Federal Financing Bank and we have long term moneys that have been taken down in that amount with an average maturity of about 14 years. That is a very positive thing for our corporation. It gives us a stable liability base and a foundation upon which to build as a private corporation.

From inception we believed that we were going to be private so we managed ourselves as a private business. We paid Federal income taxes; we have never taken any appropriations from the Federal Government. As a matter of fact, we pay a tax rate that is probably higher than any other financial institution in America. But what should be understood is that we were able to offer and price services commensurate with the cost of our money. So we have a very modest profit built into each unit of business financed by that $5 million.

Our rate of return on assets is considerably lower than very large commercial banks, for example, on an after tax basis. But that meant that we were able to offer services at a lower cost, and relatively safely, because we had an assured source of funds. Of course, if we don't manage our business carefully, if costs go up, we can have difficulties, but we took those moneys and invested them at a reasonable profit to the corporation, and at attractive prices, to the constituencies we served, and that foundation appears to be relatively safe as we move forward.

We are not making any very large profit on that. In the future, the moneys that we raise in the marketplace will have to be made available, based on the cost associated with those funds.

We just had a very successful bond issue in the last week or two, successful in the marketplace. It was the first variable ratio ever sold by a quasi-governmental entity, and the cost was relatively attractive, significantly more attractive to what we paid to the Federal Financing Bank. So the costs of our services are going to have to go up to cover those costs of financing.

Mr. SIMON. If I could interrupt—when you say relatively attractive, what numbers are you referring to?

Mr. FOX. We were financing ourselves from the Federal Financing Bank at a rate of one-eighth of 1 percent over the Treasury bill. The financing we had for 3-year money on a variable rate basis was three-quarters of 1 percent, which means an increase of five-eighths. Our earnings after taxes are less than a half of a percent. So in and of itself that increased cost of financing would put us in the red if we didn't pass along certain of those costs, or become more efficient in our operations.

But most people thought it would cost us more than that to get that issue marketed. This administration's philosophy is to see each of these quasi-government entities playing what they call on a level ballfield, that everybody finances themselves without the full faith and credit on its survivors or doesn't survive in the competitive marketplace. Fortunately for us, we have managed ourselves as a business and we were ready to take that step when it was required of us.

Mr. DEAN. Let me ask, on the average 14-year maturity date, on that debt that is one-eighth of 1 percent above the Treasury bill, what does that translate into in terms of a percentage rate average?

Mr. FOX. That is a variable rate that is predicated on the weekly fluctuations of the 90-day Treasury bill. Today, with the Treasury bill at around 13½ percent, discount, that translates into about a 14¼ bond equivalent rate, and on that we add another eighth of a percent, which would make it about at 14⅜.

In addition to that, we pay interest weekly on a significant portion of that, which means on a compounded basis, that raises that rate to maybe 14¾ percent.

Mr. DEAN. A proposal was made before this subcommittee to raise GSL interest to 14 percent and to fix the special allowance rate permanently at 4 percent. Could you comment on the problems that you would see with fixing the special allowance rate on a permanent basis?

Mr. FOX. The 14 percent is the coupon rate of the GSL in that proposal, and on top of that——

Mr. DEAN. Four percent special allowance would not be altered upward or downward with the cost of money.

Mr. FOX. So that the yield would be fixed at 18 percent.

Mr. DEAN. That is right. And then if interest rates were low, some of this 4 percent would be used to reduce the principle of a student's debt. This is Dick Cox's proposal.

Mr. Fox. I think anything that puts a fixed rate on an asset these days is incurring a degree of risk. We know that the savings institutions have been putting fixed rate, longer term assets on their books for years, and financing that in a marketplace with what is essentially very short term and therefore variable rate liabilities. Over the years these portfolios of long term assets are selling at discounts or under water and are yielding significantly less than the cost of financing.

Nobody believed 10 years ago that we would have the Treasury yielding 15 percent, yet we do. And mortgages in those days were 6 7, or 8 percent. They are still on the books of those savings institutions.

Today, financing themselves at 16, 17, and 18 percent, they are going bankrupt. This program was constructed in such a way that you have a reasonable match so that your yield on the program changes on a quarterly basis, as presumably the cost of your funds changes. That variable rate is a positive thing. It gives institutions a chance to be assured that as their costs go up, their yield goes up. As the costs go down, the yields go down. In exchange for that, they get a lesser amount of net income. This is not a particularly remunerative program for most financial institutions, but the risk has been taken out of it. I think that is what makes it attractive.

If you are asking them to put in place long term fixed rate securities, I think the banking system will walk away from it.

Mr. DEAN. What would be the impact on the corporation if there was a restriction in loan volume on new guaranteed loans to say $4 or $5 billion per year, if it were fixed so no more than that could go out in a year? Would that undermine your long term viability?

Mr. Fox. The corporation has only seen originations in excess of that for the last 24 or 12 months. We have grown tenfold over the last 4 years. The question is how you manage it. You don't manage that kind of growth. You survive it. From an operational point of view, we would probably welcome a reduction of volume because of the stresses on our system. I think that is a judgment you have to make. We can be providing whatever level of support is appropriate to whatever size market is there. I suspect if you cut the originations to that level, you have not reduced credit demand, and that demand would come to us in other directions and from other sources, for example, on the uninsured program. I don't believe that is going to cost any less or the demand for credit is going to be less because you change the eligibility of your programs.

Mr. DEAN. What are the projections for the profit of the corporation for this current year, and then 1983?

Mr. Fox. We have to be very careful as a privately owned corporation in how we talk about future profits, because of the fact there are shareholders in the marketplace. We would expect that the corporation will increase in size by about 25 percent in the coming year in terms of assets, and we would expect a concomitant increase in profitability, as a generalization.

I think it would be inappropriate for us, since there are stockholders in the marketplace out there, to make definitive kinds of projections public. We can speak to you off the record privately about that.

Mr. DEAN. OK.

The final question is one that you probably won't be able to answer, but how would you characterize the past relationship and present relationship of Sallie Mae and the state guarantee agencies, and how would you explain the fact that they are so wary of Sallie Mae and are constantly calling up congressional staffs to warn them about giving you new authorities?

Mr. SIMON. And the members.

Mr. FOX. It is curious. When we deal with most States on an individual basis we have good relationships with them. We have provided education accommodations to many of the State agencies. Quite frankly, I don't think many of them could have gotten their bond issues off without some kind of an input from us.

When you see an entity grow from almost nothing to over $5 million in size in 3 or 4 years, you have to be wary of just that. When you see that entity get legislative enhancements relatively consistently, I can understand why people would be wary.

We have provided over 1 billion dollar's worth of commitments to the States. I don't believe we have done anything prejudicial. The fees that we charge relative to our commitments tend to go lower than that which is offered by the banking industry. We are a creature of statute. We are pretty difficult to deal as we are under regulation and statute as to what our requirements are, say, for servicing. Negotiating with us frequently means a level of expectation relative to statute and regulation that sometimes is frustrating. When we are dealing with commitments that have to do with the future, in a period of time where there is apt to be change, and we are unwilling to put ourselves in a financial noose too far out, I can understand the frustration individuals have.

Also, quite frankly, in the 1981 legislation there was a great deal of misunderstanding as to just what that was going to accomplish. There was some thought we could issue tax free securities, but that was clearly not the case. There was some thought unilaterally we could go out and do a lot of things they were doing, but that is not the case. I do understand their concerns.

We try to work with the States, we continue to work with them. Many things they do are prejudicial to us. But I believe that the secondary market created by Congress exists not to be the only secondary market, but to assure that there is access in eligibility and entitlement being satisfied. If others step into the marketplace, big banks, and States to perform those functions, and that enhances the primary market, fine. We are not going to compete just for the sheer sake of competing, but to the extent we can be that secondary market or provide help in those cyclical times we are needed, we will be there. I don't think we have harmed anybody by anything we have done.

Mr. DEAN. Thank you.

Thank you, Mr. Chairman.

Mr. SIMON. One final question.

When you issue bonds, you do it for what period of time usually?

Mr. FOX. The notes that we have sold to the Federal Financing Bank range from a small strip that has a 5- to 10-year maturity, and the bulk are 15 years. When we were in the private capital markets many years ago, they were 30 days to a year. The very first bond issue we sold, we sold a week or two ago, was 3 years.

We are selling short-term discount notes in the marketplace with a maturity of anywhere from 5 to 90 days.

But what we hope to be able to do is to sell as much longer term as we possibly can. That balance sheet always has to be secure so those people who lend to us don't see the very short liabilities and the very long assets, because that is where you can be harmed. So we are pleased we were able to get at least 3 years on that first bond issue. We hope to come back to the market at least once a quarter hopefully reducing that spread I just talked about against the Treasury bill and hopefully extending the debt as long as the markets will accept it. The markets themselves are unamenable to long-term securities generally.

Mr. SIMON. You are planning these issues in such a way that you are not having too much of a roller coaster when they come due, that there is some evenness in that?

Mr. FOX. We have a relatively sophisticated financial model that shows the maturities of our asset structure. What we are trying to do is to manage our cash flow so we don't have those kinds of problems. One thing that is of a concern to me is the amount of very short-term debt sold in the revenue bond markets against lengthy portfolios of loans. The reason for that is because the rates are much lower in the short-term markets. I worry that a very significant amount of this paper is going to have to be rolled over, refinanced at some point in time. Not only is there refinancing of education notes, but there are housing revenue bonds, and industrial revenue bonds, and a whole plethora of notes going to have to be refinanced in the short term. Hopefully we learned from the savings industry experience. We are trying to manage ourselves so we don't wind up in that position where you get a big bubble that has to be refinanced and you can be in harm's way.

Mr. SIMON. We thank you, Mr. Fox, very much.

Our next witness is Dallas Martin, executive director, National Association of Student Financial Aid Administrators.

STATEMENT OF DALLAS MARTIN, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF STUDENT FINANCIAL AID ADMINISTRATORS, ACCOMPANIED BY DON HOLEC, DIRECTOR OF FINANCIAL AID, PURDUE UNIVERSITY

Mr. MARTIN. Thank you, Mr. Chairman. We appreciate the opportunity to be here. Accompanying me at the table today is Mr. Don Holec, director of financial aid at Purdue University, who is currently president of our association.

We appreciate the opportunity to be here and to discuss some of the program deficiencies that have been brought up recently in terms of the student financial aid programs, and share with you some of our insights.

I think you will admit that we have noticed recently what seems to be almost an excessive amount of criticism focused on some of the more negative features of the program. Unfortunately, we fear that that may do harm in terms of the overall perceptions of the general public, in terms of the real worth and value that the programs have had.

Certainly none of us can condone the actions of those individuals or institutions that have abused the programs or not taken their responsibility seriously. But again, I would point out I think many of the recent GAO reports and so on have tended to focus too much upon the worst case examples.

We would like to take this opportunity today to discuss some of those studies that have been done. We will try to provide a clearer picture of what can be done to provide some improvement and some suggested alternatives to the remedies that have been proposed.

One of the first studies that you have looked at was a study done by the GAO, which talks about the excessive default rate in student loans. This is a topic that has appeared before this subcommittee before. It has been a nagging problem that has been with us for a number of years. But I think it is interesting to note that in the study itself, in the very beginning, that they point out that it was nearly 19 years after this program was initiated before regulations dealing with proper diligence and standards of institutions were ever proposed.

Interestingly, the committee and Congress through the years has made a number of steps that have been designed to try to assist institutions in the proper collection of student loans. And yet, repeatedly we have delays in implementation, in the proper issuance of guidances with many of those regulations that would have been helpful.

To give you an example, the Educational Amendments of 1972 finally provided a provision whereby institutions could assign their notes to the Federal Government to assist in collection. That was very critical because institutions did not have authority to use IRS skip tracing to find lost borrowers and other ways the Federal Government had. Yet it was nearly 6 years after that was actually approved before the authority was up and operational for institutions, just a further indication of the kind of delay. That really was launched back in probably March of about 1978 when then Secretary Joseph Califano undertook a major effort to begin to try to crack down and explain to institutions that they must take their collection efforts seriously and should try to do some things. We began to see a flurry of activities that have been helpful in terms of collection of student loans since that time.

But our intent is not to just simply talk about the past. I would like to just say to you if we look at the record in terms of statistics, going back to the default rate that was in place at the time Mr. Califano began his effort, we have seen some major improvement in the overall default rate of NDSL loans.

If you look at the data that is provided in the GAO report, at that particular point in time, you would find that as of March of 1978, which was the latest data they had—June 30, 1977—the default rate was 16.86 percent. Since that time, the latest data that we have shows an overall default rate of 16.4. That clearly shows that at least the rising problem has been curbed. If you go ahead and adjust that 16.04 shown in the overall and you remove from that approximately the $215 million in accounts that have been assigned to the Federal Government, you will actually find that the default rate now for institutions for the period ending June 30, 1979 has been reduced to a figure of 11.9 percent.

So we feel there certainly has been some improvement and a lot of the continuing problem that we are facing is the fact this is old paper that is on the books that is just very difficult to work. This is evidenced by the problems that the Department of Education has had themselves in trying to work some of this old paper.

Let me point out there are a few things that still continue to constrain institutions' ability to collect these loans. Certain public institutions of this country by State statute, because of the matching requirement of the program, are not allowed to assign their assets to any other party.

Mr. SIMON. How many States are in that situation, do you know?

Mr. MARTIN. I do not have an exact count. We can try to get that. I am aware there are seven or eight, and some of those are major States.

So those institutions, even though the Department has implemented a procedure to assist in this, they are still prohibited from turning those over, or else I suspect that the overall average would be even lower than the 11.9 we are currently showing.

Second, I think some schools have become discouraged from pursuing legal action which is defined as one of the recommendations in the GAO report, due to the fact that you not only have to go through some fairly extensive kinds of legal procedures and so on, but securing a judgment against a student is no indication that necessarily they are going to continue to pay.

The reason is that oftentimes the amounts of money we are dealing with in terms of pursuing it through the legal system is such that it is probably not high priority with other individuals in relationship to other kinds of outstanding debts that are owed the Federal Government.

Third, and another issue I think has not been discussed enough, and it is probably one of the most significant factors, is the economic earning profile of an institution's NDSL borrowers. I mean by that that there are students—and clearly the NDSL program by the very nature of it being need based—we have attracted through the years those students who generally are going to have a higher financial need, and therefore, may be academically and from a credit standpoint a slightly higher risk than certain other individuals. Consequently, many of those individual students may not complete their academic programs.

Mr. SIMON. If I may interrupt you. I am going to turn the gavel over to my colleague from Minnesota. Unfortunately, I have to testify before another committee. I am going to be coming back. This does not indicate lack of interest or concern in what you are saying, or if I miss any other witnesses.

Mr. MARTIN. I certainly appreciate that, Mr. Chairman. Thank you.

Mr. ERDAHL. Proceed, please.

Mr. MARTIN. Consequently, we think that that has probably tended to have somewhat a negative impact because of the risk factor that we are dealing with here. I think that is a matter of social policy that needs to be taken into consideration when we compare this particular program perhaps with some other lending programs that it is often compared to.

The fourth thing that I think has happened in terms of discouragement by institutions and commitment is just a lack of what we would call program stability. We have had a number of cases now where several administrations have suggested the elimination of continued Federal support for this program in terms of funds. We have also had many legislative changes that have been confusing and complicated the program, the required cost of adjustments on promissory notes and collection procedures, all of those things that do not particularly encourage institutions to be able to manage these programs as well as they might.

Also, one other point is that since the history of this program has always contained a provision in the event it is ever phased out, that other than institutional matching, all of the resources would revert to the Federal Treasury. And I have to believe if there was some assurance that that money might stay with the institutions, and particularly for those that have done the best job through the years, that there might be a little more incentive to continue to put a little more effort and resources into their loan collections in that program.

Nevertheless, I think overall the program has improved. We are continuing to make improvements in it, and, therefore, I would hope that we could continue with those efforts and through the cooperation of the Department of Education.

The second area we have outlined in our written testimony I am not going to spend a lot of time talking about today, because we had an opportunity last week to appear on a panel to discuss satisfactory progress standards. I think yesterday after the representatives from the GAO discussed that, they have probably, in my opinion at least, provided some support of our logic to allow the community to develop these standards, and that the institutions and the results that were presented in that report seem to us at least to be somewhat unrepresentative of the overall quality of institutions that are out there, and the efforts of those institutions to implement satisfactory academic progress standards.

Let me skip that particular effort in the interest of time, and turn to the third area that we would like to comment upon, and that is the unofficial but still to be released control study that was recently performed for the Department of Education by an outside contractor. We have been given an opportunity to see an early draft of that particular report. We thank the Department for allowing us to review that.

I might add they have been very open, and I would compliment them, with trying to make an effort in this activity, at least the people from the program area, and certainly the Secretary's office, in trying to discuss this dilemma with us. We appreciated the opportunity.

In general, judging the overall quality control report, the draft that we have seen, it appears to us that volume I, which really comes up with the findings, is fairly well done, and is certainly much better than the earlier report done a couple of years ago.

The second volume, however, deals with recommendations for the program. I must say, while there are some interesting recommendations, it seems to me to lack perhaps some of the sensitivity and understanding of the problems and exactly how these things interact upon a college campus. I would hope we would have a chance to look at some more reasonable solutions rather than some of those advanced in that particular report.

The amount of error that is reported, both student error, institutional, and error that may occur in the processing, clearly the two areas that stand out is the amount of error caused by students misreporting data and the amount of institutional error that is caused itself by not having certain documentation or for simply not following through on certain regulatory procedures.

If you take out the failure of institutions to have on file perhaps a signed affidavit of educational purpose or a financial aid transcript which was not required at the time many of these were going on, you really significantly reduce the amount of error in the institution. So it is not as bad as it might appear in the first draft, and the Department has recognized this.

I also find, however, that the Department has had the advantage of taking considerable time and a large number of people to go out and obtain certified copies of income tax returns, to take a look at the tax assessor records, and to even look at financial lending statements from banks on individuals. And the tolerance level that they used in terms of showing errors was down to the point that any data element that showed a discrepancy by more than $2 was counted as part of the error.

I personally have found that a little surprising, that 76 percent of those students that were in the population that were studied were able to report accurately on their forms within $2, their adjusted gross income. That seems to me to suggest that most people are fairly honest and careful about the steps that they are taking. I am not certain I could do as well without going to considerable length to secure mine.

I also found it interesting that the same report shows that 81 percent of the population studied misreported by more than $2 the amount of cash or savings on hand at the particular day they had to file the form. And I suspect if those of us in this room did the same thing without calling up the bank to check that day, we would probably tend to make the same kind of mistakes.

Still, I don't mean to say there are not some findings in the report that are significant and need to be looked at.

The report goes on to point out some of those problematic kinds of areas, such as difficulty of individuals understanding what is being asked for, or difficulty in parents being able to come up with documentation for some of the data elements that are required on the form.

Still, in spite of these findings, and after making adjustments and looking at it, the Department has recently requested authority to reprogram $45 million from the Pell grant appropriation level for this year to implement a new revised set of validation procedures. The plan that they have proposed would require all eligible students to provide a copy of their IRS 1040 form to the institution. The institution in turn would review that data and compare it with the information on the form, and if there was a major discrepancy found, there would have to be information sent back to the processor for correction and subsequent adjustment of the award.

We have discussed this proposal with the Department of Education. We have certainly pledged our support to take steps to insure that we are getting accurate information. The Department has maintained consistently this will not be a significant burden upon its individuals or institutions. We would respectfully disagree with that. We suspect you are going to find a tremendous burden upon both of those parties, and, therefore, we have tried to suggest to them their may be some other ways of trying to get at the root of the problem, which is to select out those individuals that are most likely to misreport information which in turn, results in overawards.

The study goes on to report that there are some solutions that they recommend using an error prone profile to identify many of those applicants which in turn, if flagged for validation at the institution, using a simple kind of verification system of three or four data elements, could produce significant savings. This clearly would not produce as much burden as requiring every single student to come up with a copy of their income tax return.

Part of our concern is that some of the very people that the program is designed to serve may be the hardest hit with the requirement of a 1040. We have a situation that we are dealing with an educational calendar, making decisions for student awards at one time and trying to tie that to another calendar in which the Internal Revenue Service operates that do not necessarily mesh.

What may well happen is that many of what I would call the working poor in this country who will file a short income tax return, may well sit down on the evening before the deadline, fill out the necessary information on the form and ship it off to the Internal Revenue Service unaware they are going to be called upon later to provide a copy of that in the fall when they enroll for school. Those very people are probably in most cases, from families that are the least sophisticated, most likely to be discouraged in terms of this, that do not have that kind of understanding. They will be sent through unnecessary hassles to go back to the Internal Revenue Service, to obtain a copy of this and so on.

Unfortunately, the quality control study points out this is not where the problem lies. In fact, if anything, it points out these people generally tend to overstate their earnings, and thereby probably not secure the kind of awards that they should. So we believe by using something like the error prone profile and identifying those families with more complex financial situations, and in staying with a reduced but more simple set of validation procedures, that it would be reasonable and more managable to get at the basis of this problem, and not only provide better quality control in the program, which I think is necessary, but make it much easier for families and institutions overall to deal with it.

In closing, let me just reiterate our community's willingness to assist the department and this subcommittee in any way that we can to insure proper management of the Federal student aid programs.

However, we also think that the programs through the years have done an excellent job of providing educational access and opportunity to literally countless students. In our opinion, the program primarily at the present time, is suffering from two elements—one is a lack of operational stability, which does not allow for efficient planning and management of the programs at the institution or within the Federal Government; and second, is perhaps a lack of funding certainty, of not knowing, just as Mr. Fox pointed out, what to expect from year to year in terms of overall planning and staffing.

If we could somehow get to a point through some simplification of the programs and releasing some of the kind of burdensome regulations and concentrate on these two kinds of goals, and really focusing our programs on those students that need it. We continue to believe that the configuration of having a strong loan program, a good work program, and a solid grant program would be sufficient to provide educational opportunity throughout this country.

We thank you for the opportunity to be here. We would be happy to respond to any questions.

[The prepared statement of Dallas Martin follows:]

Prepared Statement of A. Dallas Martin, Jr., Executive Director, National Association of Student Financial Aid Administrators

Mr. Chairman, members of the Subcommittee, we appreciate the opportunity to appear before you today to discuss our views on the recently published General Accounting Office and Education Department evaluation reports that have been critical of the Federal financial aid programs, and to comment upon the solutions that have been advanced by the Education Department to correct "program deficiencies."

Recent publicity released by the Department regarding these reports has primarily focused upon: (1) the need to impose budget reductions to help counteract program fraud and abuse; (2) the tightening of eligibility and validation criteria to remove unworthy aid recipients who are not making satisfactory progress or who have filed inaccurate application data; and (3) efforts to correct past institutional or agency transgressions which may have contributed to excessive loan default rates and student overawards.

Since December, the General Accounting Office has released two reports pointing to deficiencies at selected schools that have either excessive NDSL default rates or insufficient procedures to implement or monitor satisfactory academic progress standards. The Department of Education has announced the findings of its most recent Pell (Basic) Grant Quality Control Report and has embarked upon a major course of action that would now require all

Pell Grant recipients to file their or their parents' latest IRS tax form with the school they are attending or plan to attend in an attempt to reduce program overawards.

An Administrative directive to recover funds wherever possible has recently prompted the Department to increase its program review activities and to bring resolution to audit findings.

None of us can condone the actions of those persons or schools that abuse the financial aid programs, nor can we criticize the Department for attempting to correct serious program errors. All of the recent activity, however, has focused upon the worst case examples and has failed to provide any comment about the positive societal aspects that have been achieved by the federal financial aid programs. Two adverse effects result from this. First, questions are raised in the mind of the average person on the street as to the fundamental validity of continuing the public investment in these programs. While it is healthy to stand back a moment and raise such basic issues, we fear the question is tainted by the prevailing negative conclusions these studies engender. The second effect, equally dangerous, is that many parents and students will unknowingly support impending program reductions because they unwittingly think they will not be affected; instead, they will hope that an effort to eliminate the undeserving will provide them with access to these programs.

Unfortunately, nothing could be further from the truth. The outcome of upcoming decisions will seriously affect the type of student who can obtain a postsecondary education and the kind of institution a person will attend. These decisions will, in all probability, affect the numbers and abilities of people who will be entering the work force in the next decade and vastly impact the socio-economic framework of our society.

Therefore, we are pleased to appear before you today to comment on these evaluation studies and hope we will be able to provide a clearer picture of what we are doing to improve the programs and suggest alternatives to the remedies that have been proposed.

The first area we wish to address is the current National Direct Student Loan default rate. The GAO report clearly reflects some of the nagging problems that have plagued all parties in recovering delinquent student loans. However, it fails to show the significant increase in recoveries and improvements made in collection practices since 1978. Factors contributing to defaults within the NDSL program can be attributed to administrative neglect at some of the participating schools and at the federal agency responsible for overseeing the program.

The GAO study emphasizes that it was nearly 19 years after the program's inception before interim program regulations were issued and enforced by the Department requiring schools to be diligent and forceful in administering and collecting NDSL's. Members of this Subcommittee are aware that several legislative initiatives have been approved by Congress in the past to reduce defaults, but all too often these initiatives have not been advanced through program regulations until a much later date. For example, the Education Amendments of 1972 included a provision allowing schools to assign defaulted loans to the Office of Education to ensure delinquent borrowers were fully notified that their loans must be repaid or they would face legal actions by federal attorneys. However, full implementation of this procedure did not occur until six years later. In March of 1976, Joseph A. Califano, then Secretary of HEW, launched a major departmental initiative to reduce loan default rates which prompted the Department to begin procedures to implement this provision. Even since then, the Department's collection activities have been hampered because of delays in developing an automated billing and reporting system, inadequate manpower to handle both GSL and NDSL accounts, and outdated, inadequate and incomplete data on borrowers.

Our intent, however, is not to exclusively focus on the past failings, but to show the improvement made in the statistics between those first used by former Secretary Califano to describe the condition of the program at that time and those reported by the GAO officials in their study of September 30, 1981.

At the time Mr. Califano wrote to all participating institutions (March 1978), the latest program data indicated the default rate for all schools was 16.86% as of June 30, 1977. By comparison, the GAO study cites program data as of June 30, 1979, (the latest date for which they had data available) showing the default rate for all schools to be 16.04 percent. This data includes about 240,000 defaulted loans, amounting to nearly $215 million, assigned to the Department of Education. In actuality if the default rate at participating schools excluded those notes assigned to the Department, the national average would have been 11.9% for the period ending June 30, 1979. While these data perhaps do not reflect the kind of improvement that many people would expect, it does seem to show that the rate is no longer increasing, that many schools are making improvements and that a substantial portion of the problem can be attributed to "old paper." The older loans cannot be collected due to improperly executed notes, or insufficient or inaccurate information as to the borrower's location. In some cases, the statutes of limitation have expired on these notes.

Still, we would like to point out the constraints which hamper collection activities. These include such factors as the following:

(1) Some institutions cannot assign defaulted loans to the Education Department because State statutes

prohibit assignment of their assets to any other party. Public institutions in these states derive their institutional matching funds from state appropriations, and therefore, cannot assign defaulted NDSL's.

(2) Schools are often discouraged from bringing suit against defaulted borrowers because many schools have pursued this avenue and obtained a favorable judgement only to find that the amount is still never paid.

(3) The economic earning profile of a school's NDSL borrowers will significantly affect the institution's ability to collect outstanding accounts. A higher proportion of students awarded NDSL's come from lower income families and are higher risk students than borrowers under other Title IV loan programs. These are students who qualify to borrow because they are needy. In many cases they come from families who are unfamiliar with borrowing in general. Taking out a loan, establishing a line of credit, is then a new experience for such a student. This factor, added to the pressures of the academic environment, can occasionally create a situation where the borrower's ability to repay the loan may not be due to unwillingness, but rather the negative impact of a multitude of economic and sociological factors upon his capability to repay.

(4) Lack of program stability discourages institutional administrators from committing needed resources to properly manage the program and adds unnecessary administrative costs that must be borne to operate the program. Since the inception of the program, the statute has contained a provision that in the event the program is phased out all resources except the institutional matching funds will revert to the U.S. Treasury. Additionally, for the last several years, nearly every Administration's proposed budget has recommended elimination of or major reductions in program funds. This uncertainty has left many institutional administrators with the opinion they should not depend heavily upon the program since they will eventually have to give up all the funds anyway. Further, recent changes in interest rates of 3, 4, and 5 percent loans and inconsistencies of deferment, cancellation and grace periods have tended to increase the administrative costs of both institutions and the use of loan servicers.

The second area upon which we would like to comment is the GAO study regarding satisfactory academic progress and the financial aid community's efforts to encourage all institutions to develop and properly monitor self-regulation initiatives that will respond to these concerns.

The GAO report was conducted by a team of investigators who, without any specific regulatory guidance, attempted to determine whether or not students were making satisfactory academic progress at the schools they were attending. Therefore, the investigators used their own concepts to determine what constituted satisfactory progress. The report admits that there are no uniform requirements among the three Federal agencies which administer financial aid, veterans, and social security educational benefits and further notes that schools having selective admissions procedures were omitted. Consequently, any student who did not have a 2.0 grade point average on a 4.0 scale was judged not to be making satisfactory progress.

Nevertheless, the report does indicate that institutions that have not yet developed an institutional policy governing satisfactory progress should do so to ensure that public funds are going to those students who are adequately completing their course work. NASFAA would only disagree with the report in that it seems to suggest that the Congress should alter the existing statute to include specific criteria similar to that found in the law governing the veterans educational benefits.

We would oppose this approach and suggest instead that the community's self-regulation standards be adopted. Such an approach can work as evidenced in past experience with the ocial Security Administration. Our Association agreed with the members of this Subcommittee during the development of the Education Amendments of 1980 that the development of standards to measure satisfactory academic progress should rest with each individual institution. Prior to the enactment of that legislation, the Title IV Committee of the Association accepted the challenge of developing an approach to the satisfactory progress issue which would not only assist institutions but would help to prevent further intrusion into institutional policy by the Federal government.

This approach began with the development of a Joint Statement on Standards of Satisfactory Academic Progress which was accepted by the American Council on Education in October 1981. During the development of the statement, personnel in the Department of Education were invited to provide reactions to the effort. Finalization of the statement brought about complete agreement from the higher education community and the Department as to not only the worthwhile nature of the effort, but as to the content and comprehensiveness of the statement. We have been assured by Department personnel of their desire to support the community's initiative and of their intent to limit their involvement in this issue.

The second phase of our approach is in the final stages of completion. In an effort to provide further guidance to institutions and to create more uniformity among their practices, the Association has developed a comprehensive monograph on the establishment of such policy at institutions. The monograph emphasizes the need for close coordination between different departments or offices on each campus in the establishment of their satisfactory progress standards. The development of such a policy at an institution not only assists in ensuring that Federal funds are being administered in a manner consistent with applicable laws and regulations, but also may influence such institutional concerns as recruitment, retention, class size and faculty workload. These factors alone emphasize the critical need for coordination and acceptance of the policy by all parties.

The monograph details the necessary steps for an institution to follow by identifying specific policy considerations and disclosure options, suggesting appeals and evaluation procedures, and by providing guidance on the implementation of the policy. Further, the monograph includes models which may be used as guides in establishing institutional requirements. The monograph will be distributed to the NASFAA membership, which consists of approximately 2,500 institutions, and will be available for purchase by other postsecondary institutions within the next few weeks.

In addition to the written publications on this issue, NASFAA has identified another avenue to disseminate the information. This approach will involve state and regional financial aid association meetings during which the issue of satisfactory progress can be addressed. The annual meetings of these associations will also provide a forum for discussion.

Given the community's efforts and the Department's support, we would urge the Congress to give the postsecondary education community the opportunity to implement their own standards rather than attempting to enact complicated and arbitrary standards that will undoubtedly tend to penalize students in some programs.

The third area upon which we wish to comment is the recently completed and as yet unofficially released Quality Control Study performed for the Department of Education by Advanced Technology, Inc. While we have not had an opportunity to see the final product, an early draft of the study was given to our office for review. Therefore, the comments I make regarding the quality of the study are simply my own perceptions from reading the draft study.

In general, the overall quality of the study appeared to be more thorough than the earlier study conducted for the Department.

Volume 1, a report on the study's findings, is certainly superior to Volume 2 which provides suggested corrective actions. Unfortunately, the recommendations in Volume 2 seriously understate the administrative burdens and complexities which, if enacted, will be imposed on all students and all institutions. This is not to say that the findings in Volume 1 are totally acceptable. For example, if you excluded from the institutional error calculation the fact that an affidavit of educational purpose and financial aid transcript could not be found, the institutional error would be significantly reduced. It is also interesting to note that discrepancies were noted if the item reported differed with the item verified by more than $2.00. It is important to keep in mind that the contractor had the advantage of taking a considerable amount of time to collect this data from certified copies of parents' and students' income tax returns, financial lending institution statements and from tax assessor records, all of which would constitute hard documentation. Yet the contractor had just as many problems as schools in verifying those data elements which can only be substantiated with soft documentation. Soft documentation includes handwritten notes and verbal assertions. As such, it is interesting to note that in spite of the intensive work done by the contractor, there really isn't hard evidence to substantiate the validity of many of the data elements collected, e.g., Did you live with parents for more than six weeks during 1981?

The study also shows that 76% of the population were within $2.00 of their true adjusted gross income which seems to support the contention that most people are honest and take great pains to report their data correctly. Using the same tolerances, a comparison with official bank statements, showed that 91 percent, of the population studied, misreported by more than $2.00 the amount of cash and/or savings on hand on the date the report was filed.

The findings in the report, in addition to identifying the most discrepant data elements, also cited the data elements that most parents and students indicated were the most problematic and difficult to understand or to answer. Parents noted a particular problem with documenting the market value of their home and its current equity. Students cited particular problems in obtaining parents' income tax data for applications. Both students and parents mentioned that it was very hard to predict future family earnings, answer questions about supporting students or predict school year income for the upcoming school year.

Still, in spite of these findings, the Department of Education has recently requested the authority to reprogram $5 million in program funds available for the Pell Grant program in FY 82 which they anticipate will be required to implement a revised set of validation procedures. With these funds, the Department proposes to change the current validation procedures to include the requirement that all eligible applicants submit copies of their or their parents' IRS tax returns to the school they are attending or plan to attend so the financial aid administrator can verify the adjusted gross income and federal income tax paid with the original data provided on the application form.

It should be noted that personnel within the Department of Education have discussed their plans with representatives from the postsecondary education community. We, in turn, have expressed our support to take steps which will help to ensure that more accurate information is being collected. We have questioned, however, the necessity of imposing such extreme measures upon all financial aid applicants and taking additional dollars from already limited program funds to pay a central processor to perform work that generally should already be covered in the original contract.

The Department has also maintained that by limiting the verification to only two data elements it will not impose any significant burden on institutions and will, at the same time, achieve significant savings in the Pell Grant program. Further, they suggest that these steps will not create hardships on students and will in fact help ensure that some low income students will actually get larger awards to which they are entitled.

We respectfully disagree with the Department's contentions and feel that such drastic measures are uncalled for at this time. Our fear is that these procedures will create unnecessary hardships on the very students the program is primarily designed to serve.

The data from the Quality Control Study clearly shows that recipients in the lowest verified income category are the most likely to overstate their adjusted gross income thus producing smaller awards than those to which they were entitled. Conversely, however, there is a substantial number of students who under-report their income data thus providing them with awards greater than those to which they were entitled. Therefore, it is difficult to argue with the Department that something should be done to prevent money from going to students who should not receive it. However, it is equally important to ensure that truly eligible students receive the awards to which they are entitled without instituting barriers that may make it difficult if not impossible to prove that they have provided correct information. Unfortunately, data provided on the application is self-reported and can only be verified by comparing it with the information submitted to the Internal Revenue Service. Regretably, many of the working poor who file a short form often complete the tax return themselves and mail all of the information to IRS without keeping a copy for themselves. While people can later obtain a certified copy of their return from the IRS, it requires additional effort and the filing of forms that will in many cases substantially delay receipt of the required information by the institution. Schools held liable for errors made due to unverified data will be reluctant to make a payment to the student until they at least have a copy of the required tax return. Consequently, students from poor and unsophisticated families will be the most likely to be caught in this catch 22 which may discourage or prevent them from going to school. Additionally, there will be other students who cannot legitimately provide a copy of their parents' latest tax return because their parents have secured a filing extension or simply refuse to provide a copy of the tax return to the school on the basis that such is an intrusion into their individual privacy.

The Department's proposal is well-meaning, but unfortunately it is tied to the Internal Revenue System's calendar which is not compatible with the time frames that must be met in the student aid delivery system. Complete implementation of these procedures within this coming year will create significant time delays and enrollment disincentives for many students.

Considering that we have already announced application procedures and distributed student aid applications for this coming processing year, it appears to us that the Department might well consider using a different approach for this processing cycle. The Quality Control Study suggests that by using specific edits an error prone profile could be established in the processing system to identify those students who are most likely to have filed incorrect data. This procededure could be used by the Department to identify a reasonable percentage of student applicants who in turn could be required to submit verifying documents and/or statements to schools before awards are disbursed. While this system is not unlike the current selection process, the Quality Control

Study suggests that such an approach could certainly do a better job of identifying those students who are most likely to be in error. Additionally, the current validation process could be substantially modified and attention focused on those 4 or 5 data elements that will produce the most significant savings. We also feel that the Department could then work with the community during the coming year in developing pilot validation programs which in turn could begin to suggest the most efficient and least onerous methods of securing the most accurate information.

In closing let me reiterate the community's willingness to assist the Department and this Subcommittee in any way to ensure the proper management of Federal student aid funds. Our goal and yours has always been to ensure that truly eligible students have the opportunity to achieve a postsecondary education.

Again, let me thank you for the opportunity to comment on these issues. I will be glad to answer any questions you might have at this time.

Mr. **Erdahl**. Thank you very much.

We have been joined by Congressman Weiss. Ted, do you have any questions at this point?

Mr. **Weiss**. I do not at this time.

Mr. **Erdahl**. What about counsel?

Ms. **McAdam**. Dallas, you said there could be better solutions to the study put forth. Do you have any specific ideas on what would be better ways of addressing the problem?

Mr. **Martin**. Well, currently in the Pell grant program, for the last 2 or 3 years there has been in place a requirement of validation, whereby out of the prime processor, they look at through a series of audit checks in the system, interrelationships of certain data elements to try to identify whether or not they are accurate.

For example, they will take a family's adjusted gross income, the number of people in the family, the amount of Federal income tax paid, and run a quick model to see whether or not those figures line up. If it is found they are out of line, there is an automatic flag to tell you not what is wrong, but it is a clear indication that it does not fall within the tolerances expected, using the IRS tax tables. So those have been developed.

Quite frankly, what the error prone profile and the quality control study suggests is that you many not need as many audits. They have identified those people who are more likely to have perhaps made error or have error involved. Clearly, people that are itemizing their income tax returns and are applying the usual kinds of procedures that can occur with the tax system, are more likely to be understating income, and thereby perhaps securing overawards, than are the lower income students that are identified in the population.

If you go on and take their recommendations from that study, it appears that if you—I might add we are currently doing validation from the Department on about 300,000 applicants a year, whereby those come back and are flagged and institutions validated. That is about 15 percent of the total applicant pool of the eligibles.

The quality control study seems to suggest to me that you could with a very slight increase in that number, and by looking at fewer data elements, you could continue to flag somewhere in the neighborhood of 350,000 to 400,000 of those students using different criteria and you could get a significant number of those that fall into the error prone range where there may be overawards, thereby reducing any misrepresentation in the program.

At the same time, you would not be overloading the current systems, it is with the processor, because of increased corrections and back and forth documentation, nor the workload necessary at the institutions, because you would be keeping the cost and number of what is going on at the present time about the same.

We have currently undertaken a survey of our membership on the amount of validation activities that are going on over and above the requirement that is imposed by the Federal Government. We expect to have the results of that survey available within the next week to 10 days. We have assured the Department of Education we would be more than happy to share those results with them and be happy to provide it for the record here.

But it is clear to us schools are making additional efforts on their own in many cases. I suspect if institutions had a little more authority in terms of those cases where we really find there may be something wrong because of other information that we have, other than being locked into a set of rigid requirements, that again institutions would be more willing to assume some of this responsibility to try to prevent any error. It is obvious to all of us we do not have enough dollars to serve the students we would like to at the present time.

Mr. **Erdahl**. Thank you.

Mr. **Dean**. If I could ask you to comment a little bit on the possibility of Sallie Mae getting involved in nonguaranteed loans that are made by institutions, would you welcome such an activity on the part of Sallie Mae, and have you heard from a lot of schools that are anxious to start making such loans to meet the unmet need of a lot of students?

Mr. **Martin**. Mr. Dean, I would say we certainly have been receiving an increased number of inquiries from institutions. I would say it is primarily from independent institutions, although some larger public universities are equally concerned. I think there is a general kind of fear, trepidation, paranoia, in the postsecondary education community right now about what happens if we suddenly take this large credit system we have available through guaranteed student loans and it is dismantled or substantially reduced.

I think institutions fully realize that a credit system is necessary in order to preserve enrollments and to provide the opportunity for parents and students to meet rising educational costs. So, yes, they have been looking at alternative sources.

There are a lot of people out in the marketplace right now, various investment bankers and people selling revenue bonds and so on that have been, I guess it is safe to say, spending a lot of time discussing this with institutional representatives. And clearly, if some of those things are going to work, it appears to me there will have to be some secondary markets to perhaps make those attractive. So I think it may be an appropriate role for them to look at. But I also am concerned that the primary purpose of the GSL program, if we are going to maintain that with some subsidy for students who may not have access to some other sources, students who cannot afford loans at market rates, that we continue to provide at least the good role that I think Sallie Mae has played in providing security and the availability of that capital out there.

But I would not put myself in a position to say they should not explore the others and look at them very carefully, because they probably have much more expertise than do many of the educational institutions in knowing whether those are desirable plans and whether or not they are secure, than perhaps do some of the other people that these things are being discussed with.

Mr. **Dean**. Are schools telling you they are going to go ahead and make such loans whether or not Sallie Mae will buy them?

Mr. **Martin**. We have some evidence from a few institutions that are pursuing alternatives at this point. I only know of probably four or five that are actually beginning to take up that role. Most of them are hopeful there will be an outlet down the road, Sallie Mae or some other source. But beyond that, I really cannot say.

Mr. **Dean**. Would I be correct in assuming that a lot of community colleges and a lot of colleges serving largely low-income students would not be able to get into these loans at all?

Mr. **Martin**. I think that is a very safe assumption. They do not have in most cases the kind of portfolios or reserves within those institutions to provide the security that is necessary for these bonds and other kinds of financing mechanisms. So you pretty well get down to those that are more established or broader based.

Mr. Holec might wish to comment on that in terms of experience, because I know his institution has been for another reason looking at some alternatives of financing. Purdue, of course, is a large State university.

Mr. **Holec**. I think right now one of the concerns is just what is going to happen. Everybody is looking at a variety of options, a what-if situation. What if the program is changed in certain ways, and if the credit market begins to dry up? What are the alternatives there—getting back into lending as an institution under the guaranteed student loan program which used to take place at our institution as well as others, the secondary market—just a whole variety of arrangements.

So I think at this point it is mostly discussion and exploration of if the worst comes about, what kind of other alternatives might be available to turn to to help students in financing their education.

Mr. **Dean**. What percent in Purdue right now is being recycled into aid?

Mr. **Holec**. As a percent, I am sorry, I cannot give you right off hand. Out of current revenue funds, the university is putting in about $1,300,000 currently for undergraduate students. That is grants based on financial need. Then in addition to that, there is support that goes to graduate students and the like. I can get that for you and provide it.

Mr. **Dean**. I think that would be worthwhile for the subcommittee to have.

If I can ask Dallas, do you find a trend among institutions to make fewer grants and to get more into loans to students so as to make the dollars go further?

Mr. **Martin**. I think there are a number of institutions—again I think this is more likely to be occurring within the independent institutions because of the large differences in tuition costs, because of the lack of State subsidies to make up that difference—I have had a number of those individuals recently who have shared with me that they are beginning to look at, could they use some of their existing assets that typically have gone in the form of grants, to leverage other kinds of funds, or perhaps to use some of that through financial markets to help pay part of the interest subsidies for the students.

I think they are very, very concerned that given our current economic climate, with interest rates being as high as they are, most people recognize that students are not in a position to repay interest on the loans while they are in school. So you have a deferred period, giving them an opportunity to get on their feet.

When we start talking about loans at market rates, where we are talking 14, 15 percent interest rates, and the compounding effect of that very quickly creates a debt burden that is substantial.

I look at students coming out now with student loans that literally are paying interest rates that are much larger than I ever paid for my first home. We have all been experiencing that. I think it is frightening. I am very fearful that students in many disciplines simply will not have the earning capacity, at least early on, to deal significantly with that debt.

Schools are looking to see, can we somehow share that so that the student is going to continue to pay a significant portion, because we use part of our money to help them out, so we are not going to be creating a whole generation of indentured servants.

Mr. **Dean**. Relating to a comment in your testimony regarding state statutes prohibiting assignment of loans to the Department. Would you like to see the Congress preempt the State statutes?

Mr. **Martin**. Constitutionally, I don't think you would be able to do that. That would be an easy way to do that. I suspect we get into some differences between State statutes and the Federal Government.

What I was trying to point out on that, is that even though we have created some incentives here, and I think it was a very wise and helpful situation of creating the assignment of these loans, I am disappointed that for a period of time to try to assist in this effort, when Mr. Cornfeld, who was involved with the effort with Mr. Califano, they established a procedure of what was known as a referral process through part of their assignment.

The referral institutions could give some of those notes to the Department of Education. They, in turn, would try to assist in the collection. And then the money that was collected was returned to the school to deal with this problem of not being able to assign the assets.

The Department has now eliminated the referral provision of that, and it is only a straight assigned provision. So it now totally precludes those other institutions in those States from turning over those loans. So I think it might be helpful to talk about at least, or discuss with the Department again the possibility of doing referrals which would relieve some of that. That might be one possibility.

Mr. **Dean**. Thank you very much.

Mr. **Erdahl**. Thank you, Mr. Martin.

I believe you were here yesterday when we heard from several people from the GAO. As you state in your testimony, I think some of the standards they talked about are reasonable, having these loans and assistance available for students who actually are students, and having some type of satisfactory academic progress. I thought it was ironic, that, as I drove home last night, the news picked up the story. We can guess the part of the testimony they picked up was about the second semester sophomore who had been in college 5 years, and the person who flunked accounting six times. That was the story in the news. I think those are not the normal procedures, yet those are the sensational things.

I am going to ask what may be an unfair question. You mentioned several times what the Department was about in all these endeavors. Do you have any hunch or clue whether these functions might be administered on the Federal level under the new, whatever it is going to be—I will call it the Federal educational entity.

Mr. **Martin**. I don't want to discuss the structure any more than you do, Mr. Erdahl. I would say that it is our opinion there are a number of very dedicated and qualified individuals who are currently working in the current structure within the Department of Education and formerly the Office of Education who understand and have an appreciation of these programs and have done that. It seems to me some of these functions must be centralized and must be dealt with through that kind of entity, whatever it is.

I also believe, however, we could probably improve the system somewhat if in fact the educational institutions who are the people on the frontline that have to deal day to day, face to face with the students had some additional discretion and some additional authority in some of these matters. We have been trying to work as an association in terms of taking responsibilities to develop our own standards and our own self-regulation initiatives to improve this.

One example of this that we might point out which might be very carefully looked at is, I wonder if, given the fact that 80 or 85 percent of applicants for Pell grants are currently getting into that system by applying through one of the multiple processors or satellite processors contracted with the Government, those agencies that have already typically been performing that service.

And second, institutions in all of the other programs have discretion in terms of putting that together. It seems to me that there might be an area where we could begin to look at, some examination that could provide decentralization back to the institution with some responsibilities, eliminate some of the middlemen and some of the steps in the processes. That would not only save substantial amounts of operational costs and personnel, but would return some of the control back to the campuses where they are dealing with the students and where they can provide that helpful hand.

Along with that is the assumption there would be some discretion, because many of these things are simply not into a category that it is all one way or all the other. I think institutions would accept that responsibility, would do it well, and that we could save money and make the process smoother and easier for everyone, and perhaps add greatly to the simplicity of the current system.

Mr. **Erdahl**. That sounds sensible. We have also heard rumors that maybe the loan and grant function would be transferred to the Treasury Department. Do you have any reaction to that?

Mr. **Martin**. I would sincerely hope, I guess—and this is certainly not an official association position, we have not discussed this—but I think we are concerned that we do not totally fragment all of these programs. I have great respect for the people in Treasury, and their ability to perform their functions that are currently assigned to them. But I am not certain people over there are in the best position to look at overall educational policy, which I think has to be the basis of these programs. While they may know a great deal about credit management and financing, I am not certain they would have the same kind of sensitivity that I think people in the Department of Education have in terms of looking at the investment that we are making and the kind of support we are building for our postsecondary educational system.

Mr. **Erdahl**. Thank you very much for sharing those observations with us.

Mr. **Weiss**. Mr. Martin, do you have any information or perhaps insight as to the impact of the changes which we made in the guaranteed student loan program last year on the lending institutions and their reaction, and on the students? Perhaps you have more on the first than the second.

Mr. **Martin**. Yes, Mr. Weiss, No. 1, it is safe to say that last year as we completed the omnibus budget reconciliation and incorporated into that the changes in the guaranteed student loan program, you are well aware that those provisions went into effect on October 1 last year. Consequently, in anticipation of that, I think most students and most institutions participated in informing students there was a change forthcoming. So probably about 95 percent of those students that secured loans did so in advance of that date. Consequently, the changes by going to the $30,000 income cap, the new 5 percent origination fee, the minimum loans and so on, we are just now beginning to find out from students how they are reacting, from a few enrolling in second semesters that did not secure loans before.

Of course, that means the real savings that would be incurred from any of those kinds of procedures have not yet shown up on the ledger sheets.

As we approach this spring, and institutes begin the process of reapplying for funds for the coming academic year, starting July 1, certainly everyone now will be subject to those new provisions and wading through it.

As we get into the spring, we will begin to see very clearly whether or not those tightening of eligibility requirements will in fact not only save the money anticipated, but whether or not create unnecessary hardship on certain classes of students.

As far as the lending institutions are concerned, while I do not feel totally prepared to speak a long way on this, in conversations that I have had, I would say that part of what they experienced that made it somewhat difficult was this tremendous rush on the banks that occurred late last summer. Consequently, they were just inundated with papers and forms and so on which did not provide the normal kind of flow of applications.

So, from the management standpoint, many of those people have had to really dig their way out of that procedure, and that has not been without obviously additional cost and problems.

I suspect now if we are into this under a normal flow, their operations will get back to a more predictable level, as they were before. But I think it is a little early to say whether or not we were successful with the changes we made and what impact they will have on overall cost to the Federal Government as well as upon volume and participation by people in the program. My belief still is that it will reduce expenditures and will provide savings. But we are not going to really see that until later this year.

Again, Mr. Holec might wish to comment on that because he would have firsthand experience in terms of the kind of application flow he has seen.

Mr. **Holec**. Very clearly all of the applications or a very high percentage of them, were in before the cutoff date. I think we processed on our campus 12,000 applications before October 1. Since then, only about 600 or 700 have come in. Several of them, many of them, have been denied, although I cannot give you the exact number. I think one of the very real concerns all of us have in the field right now in trying to advise parents and students about financial aid for next year is having to say we cannot tell you anything, we don't know what student aid will look like next fall.

Part of that problem stems from the Pell grant program. The processing of those forms has not begun. There are indications it may be another month or two before that may be started. The procedures for validation which should be in institutions' hands at this point, because they have the financial aid forms, are starting to get applications and starting to review and process them, the decisions regarding what that is going to be like are unknown. So our hands are tied in terms of getting applications in the Pell grant system.

In the guaranteed student loan program, we are precluded from processing any guaranteed loan application for any academic period beginning after July 1. Students are coming in beginning to inquire about that. We have to say you are going to have to sit tight, we don't know, we are waiting for the family contribution schedule, or curves or tables, whatever is going to be used by the Department for this next year. And until then, we cannot begin.

So I think there is a tremendous amount of indecision and inability on the part of institutions to talk reasonably with students and families about what to expect for next year.

I look back through the several years—I have been in this business 16 years—and the last several it is always like the crisis comes in the summer. All I have been able to tell my staff is we will have another crisis in 1982. We have to face this, students and families are going to have to make some decisions. That may have as much impact on volume as anything. If decisions are not made, because we can't tell students until June, July, August, September, after school starts, what their aid situation is—they are going to have to make some decisions before then, and many are going to decide, have to face reality and say "I cannot go to school."

Mr. **Weiss.** Thank you. Thank you very much.

Thank you, Mr. Chairman.

Mr. **Simon.** We thank you very much.

I call on my colleague from Minnesota to introduce the next witness.

Mr. **Erdahl.** Thank you very much.

We will ask Mr. Ingle to come up to the table.

While he is relatively new in his position, the unit he represents has not only been recognized in Minnesota but throughout the country as a good entity in doing what it says and coordinating higher education for the State of Minnesota.

I am very glad to welcome Mr. Ingle today.

STATEMENT OF CLYDE R. INGLE, EXECUTIVE DIRECTOR, HIGHER EDUCATION COORDINATING BOARD, ST. PAUL, MINN.

Mr. **Ingle.** Mr. Chairman, members of the committee, I am pleased to be here. I welcome the opportunity and the invitation to speak to you.

I have been invited to speak on a relatively narrow part of the problem of how parents and students will finance their postsecondary education; that is, specifically loans, and a little more specifically the importance of the secondary market for those loans.

I would like to preface my prepared comments, if I may, by noting that on behalf of the members of the Coordinating Board in Minnesota, Minnesota students and institutions, and postsecondary education in the State, we would like to express our appreciation for the support and expression of our concerns that Mr. Erdahl has made. We recognize that, and we are very appreciative of that here.

The second comment I would like to make before I move to my prepared comments, which members have a copy of, is that I cannot resist, if I may, Mr. Chairman, a slight response to your question of what would you do if you were to restructure the financial aid system.

The fact is that responsible authorities in Minnesota today are heavily into debate about just that question at the State level. I think it is critical, as I know you are aware, to recognize the difficulty facing a State as it tries to protect its goal of promoting equality of opportunity for an education which best suits the needs of its citizens. We are engaged in that debate currently.

Still, the major investment in postsecondary education in Minnesota and in most States does come from the State level, and one of our critical questions is how we relate to the Federal presence, whatever it may be.

I must say that in our judgment this really becomes a question of values. It is not so much a question of rules and regulations, as onerous as they may be. It is a question of what we as a society are willing to pay for this process of postsecondary education and where it is best to be put.

Having said that—and I would welcome an opportunity to speak further on it—I would like to turn now to my prepared remarks.

I will offer a bit of background as to why I am going to speak on this particular issue. I will speak briefly on the importance of the secondary market for an effective lending operation at the State level and elsewhere, and then I will speak specifically to some concerns that we have.

The coordinating board in Minnesota is an 11-member lay board designed to represent the public at large in coordination of post-secondary education in our State. The board has broad planning and research responsibilities, as well as administrative duties. We are responsible for a number of State-funded financial aid programs, as well as the second resort direct loan program under the Federal guaranteed student loan program.

Our direct student loan program is one of the largest single tax exempt lenders in the Nation, anticipating disbursements of over $100 million this fiscal year. As we discuss mutual interests this morning, it is essential that you understand that our program is designed to provide access to loans for any eligible Minnesota student who is unable to obtain loans from commercial lenders. As such, we have made between 45 to 55 percent of the loans in Minnesota since the inception of our program in 1974. During this period, we have made $340,561,000 in loans.

The Minnesota program is capitalized by the sale of tax exempt revenue bonds. Since April 1974 the board has issued bonds of $491,850,000 and today has outstanding obligations of $332,000,000. This debt is the sole obligation of the coordinating board and is not backed by either the credit or taxing power of the State.

We believe our program is a prime model of successful management and use of the tax exempt market for a wholly public purpose. Our students and postsecondary institutions are dependent upon the timely availability of this credit as an integral part of their financial aid system.

Without the availability of these loans many of our students would be unable to attend the program suited to their ability and aspirations. The result would be both distortions and declines in enrollments.

As to the importance of a secondary market, the ability of the coordinating board to fund a student loan program of last resort as directed by the Minnesota Legislature, is critically affected by the presence of an effective and reasonable secondary market for student loans.

With the existing arbitrage requirements and the growing demand for loans, it has always been difficult for the board to keep much ahead of quarterly loan demand. Thus, our cost of capital has been at about current tax exempt market rates and we have shared the vagaries of the market for the past 8 years.

This has meant that our margin for operation has been very slim at times, particularly since the special allowance formula was changed to one-half the standard formula yield.

By standard measures, I think most would classify the Minnesota program as financially mature and stable. Nevertheless, it is apparent that under most market conditions our offers of debt need some security in addition to scheduled loan repayments and current guarantees.

In our judgment, this need can most effectively be met through a long-term relationship with a secondary market for student loans. If this need exists for a mature and stable program, I am sure you can understand how critical the need is and will continue to be for programs just beginning to use tax-exempt capital or those in the process of maturing.

In this context, the secondary market serves simultaneous dual functions: Debt security and fund liquidity. Both functions are secured by the commitment to purchase loans if and when the program needs to sell whether to meet debt service requirements or to provide capital for additional loans.

As market conditions restrict borrowing to short-term high interest borrowing, these functions become absolutely critical. To meet these needs, the secondary market must be available, flexible to program circumstances and affordable.

The commitment to meet these needs must be unequivocal and not subject to alteration with minor or short-term market fluctuations. All parties must understand and appreciate the fact that tax exempt fund loan programs are most dependent upon secondary market services during periods of general market distress or uncertainty.

The Minnesota program has had a long relationship with secondary markets and with Sallie Mae in particular. We have had dealings with Sallie Mae since 1976 and in 1979 we signed an historic agreement which was designed to cover up to $200 million on loans made from our program.

We have used up the amount in that agreement and we have been unable to negotiate either an extension or successor to it on terms which we feel are reasonable.

Therefore, we have turned to private lending institutions where we have been able to secure limited commitment agreements in terms more responsive to our needs. However, as fiscal condition continue to change, we have no assurance that these options will be available to us in the future.

The 1979 agreement provided long-term security and with it flexibility to effectively respond to student demand within a wide range of market conditions. Without such an agreement, we will be increasingly dependent upon short-term financing and the ravages of changes in short-term rates.

As our experience indicates, Sallie Mae can and has served as an effective secondary market for programs capitalized, at least in part, by tax-exempt debt. However, for more than 1 year now she has not offered services or terms which are responsive to our needs. I think it is also important to note that there is no indication that the private alternative will continue to be available.

I would now like to speak more specifically with you about some concerns about the future role of the Student Loan Marketing Association as a principal secondary market opportunity for student loans in the Nation.

I must stress to you that I speak today not as an investment banker or financial analyst or as a bond counsel. I speak as one who has the responsibility to the board, the Minnesota Legislature and more than 50,000 students annually to insure that sufficient funds are available for students and their families to pursue the postsecondary education of their choice.

Thus, my perception and concern is a very practical one, not confused by the intricacies of the bond market or the legalities of bond sales. It is how we are going to meet the needs of Minnesota students and families at prices and terms which are reasonable and which protect the long run integrity of the program and the public interest.

At the outset, then, let me state an assumption which I believe to be fundamental to the concerns of the committee.

It is my understanding that the central purpose of the Student Loan Marketing Association is to offer liquidity to commercial and direct lenders. It was within this understanding that 1 year ago my colleagues from a number of other States and I expressed our concern about the additional authorities and responsibilities for Sallie Mae which were ultimately adopted by Congress.

While I do not propose to reopen the debate about the individual amendments, I do think there is a critical question which I believe this committee should address as a part of a continuing effort to insure that students are able to secure adequate resources to pursue a postsecondary education.

This question is whether the additional authorities and responsibilities are directly in conflict with the central purpose of the Student Loan Marketing Association. I think that the presence of an effective secondary market for student loans is absolutely essential if it is our intent to provide credit to students and families.

I believe that the central and original purpose of Sallie Mae was laudable and that the underlying working assumption that Sallie Mae should function in the competitive market is sound. I would like to stress that.

However, the very competitive principle which guides Sallie Mae's original purpose when applied to the additional authorities could determine the secondary market function, which I understand to be the central purpose of SLMA.

In practical terms, the question is whether SLMA's interests might better be served in the future by exercising its new authorities to become a lender, a secondary market for unsecured loans, or a seller, purchaser or underwriter of tax exempt student loan bonds.

To achieve these objectives Sallie Mae could demand terms and conditions as a traditional secondary market that would undermine statewide direct lenders and private nonprofit programs.

If this potential exists, it seems to me that a potential for conflict of interest exists which could result in behavior contrary to the long-range purpose and intent of national policy.

In short, and in simple terms, the purpose of serving as a secondary market to all types of lenders may well be in direct conflict with the additional authorities provided Sallie Mae in the reconciliation bill.

In my judgment, there is a direct conflict of interest here which does not make for effective or efficient policy in the long run. Let me stress here that this is not a conspiratorial view of the world.

I believe that the intentions of all involved from Sallie Mae to Members of Congress are the best. However, I do not expect that individuals will remain in their present positions forever.

Based on our experience to date, I expect that the conditions for funding the student loan programs will become more difficult. Let me stress here that if it is difficult for a mature program such as Minnesota's it is going to be even more difficult for those programs which have evolved over the past few years, and I would think that this would be of particular interest for this committee.

Thus, the potential for conflicts of interest and purpose which I perceive here seems to me to bode ill for the efforts of States to provide credit to students, which I understand to be the intent of Congress from 1978 and still to be the case today.

Again, the conflict between serving as the principal secondary market and the incentives which surround the additional authorities now held by Sallie Mae seem to me to represent the potential for a conflict of interest which will, in my judgment, work to the disadvantage of the States which are attempting to responsibly deal with the financing needs of their students.

Mr. Chairman, I think a serious attempt to address this question and related ones will again assist the committee in the constructive process of clarifying to the staff and board of Sallie Mae what Congress intends as a priority role for Sallie Mae.

At the same time, this effort will establish a basis for future evaluations of performance. Without such an effort on the part of you and your colleagues, Mr. Chairman, I fear a period of confusion characterized by needs inadequately addressed, unproductive tension, conflicts of role and interests, and ultimately the placing in jeopardy of that part of the GSL that has been responsive to the needs of students that the traditional commercial lenders have been hesitant to meet.

I want to thank you for the opportunity to join you today and to share these concerns with you. I would be pleased to assist you and members of the committee in any manner which might be helpful.

Mr. SIMON. Thank you very much for your testimony.

I gather that you are suggesting that there should be statutory changes for Sallie Mae. I wonder if you could be more specific in what you would like to see.

Mr. INGLE. Mr. Chairman, members, I am not proposing statutory change. I am concerned about the lack of clarity as perceived by those of us who are responsible for providing capital at the State level for programs, for students.

Mr. SIMON. Are we talking about a communication problem, then?

Mr. INGLE. I think it is a question of what is the ultimate use of the authority which is currently, as I read it, in the legislation. I am not proposing statutory changes.

Mr. SIMON. Let me again, for purposes of clarity—where you say, "To achieve these objectives, Sallie Mae could demand terms and conditions as a traditional secondary market that would undermine statewide direct lenders and private nonprofit programs."

Can you spell out more specifically what you mean there?

Mr. INGLE. Yes, I can.

I think the simple way to state this is as follows: If one of your major servicers in any kind of activity is put in the position of being a competitor in the major activity one is engaged in, then clearly the incentives, it would seem to me, which underlie the competitive mode of operation for Sallie Mae, which I applaud, would push that organization over a period of time to demand terms and conditions of lenders, especially tax exempt lenders, which would be to the advantage of the organization not to have to deal in the secondary market.

Mr. SIMON. Can you be more specific? Let's use a concrete A-B-C example.

Mr. INGLE. Sure. With the end of the commitment to purchase, the commitment agreement which we need for two purposes: One, in order to provide liquidity for our program and second, to be able to go into the private capital markets. We need ratings to be able to sell at competitive rates, interest rates, we need a commitment agreement.

We have not in the last year and a half been able to work out an agreement with Sallie Mae which we think is reasonable in terms of the ultimate cost to us.

Now, I think—and I agree with the comments of Mr. Fox—the principle of operating in the competitive market is one that may make that necessary. If that is the case, that is that the terms are such that they will ultimately drive the lenders such as the program in Minnesota out of business, then the question comes how is the State or the Nation to provide that credit.

I don't know the answer to that, but I know that we must have the commitment to purchase. If the terms being provided to us are such that they make it unprofitable and impossible for us to secure funds and lend at a break even point, which is our objective, then the effort of the State of Minnesota is ended.

Mr. **Erdahl**. Mr. Chairman, this is very technical. I have a question in the same area.

On page 3, up at the top of the page, you say, "As our experience indicates, Sallie Mae can and has served as an effective secondary market for programs capitalized at least in part by tax exempt debt. However, for more than a year now she has not offered services or terms which are responsive to our needs. I think it is important to note there is no indication that a private alternative will continue to be available."

So, really two questions, if I might, Mr. Chairman.

Could you be more specific, where you say she, meaning Sallie Mae, has not offered services or terms which are responsive to our needs. Then the other thing about the private alternative, which is something we hear much about in Washington in recent weeks and days.

Mr. **Ingle**. Yes. The simple explanation here is that from our perspective the demands of the Student Loan Marketing Association, as we worked over the last 2 years, would have provided Sallie Mae with what we consider to be perhaps an unreasonable high yield which would have meant fewer resources left in our program to be linked to students.

The specific details of our difficulties are very technical. What I would like to do is provide those written for the record and not try to explain those here because they are technical details. I will be glad to do that.

[The information follows:]

APR 6 1982

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OFFICE OF THE EXECUTIVE DIRECTOR

1 April 1982

The Honorable Paul Simon, Chairman
Subcommittee on Post-Secondary Education
U.S. House of Representatives
320 Cannon Office Building
Washington, D.C. 20515

Dear Chairman Simon:

I was very pleased to appear before your committee on February 4, 1982 and am especially appreciative of the opportunity to respond, for the record, to the major question which you posed at the hearing: What are the specific problems with Sallie Mae's service, or lack thereof, to statewide direct lenders that capitalize their programs through the sale of tax-exempt bonds?

Background

As I said at the hearing, an adequate response to this question is both complex and technical. To be sure we all understand the context of the question I want to review, again, the basic characteristics of the Minnesota State Student Loan Program (MSSLP):

> Purpose: To act as a second or last resort lender for those eligible applicants who have been refused loan access by a commercial lender.
>
> Origins: Authorized by the 1973 Minnesota Legislature to link directly with the Federal Higher Education Act, as amended. Subsequent changes have been made to conform with changes in the Federal Guaranteed Student Loan Program (GSLP).
>
> Volume: Since 1974 the Minnesota Program has made between 45 and 55% of all Minnesota loans totaling more than $340 million. During this fiscal year, ending June 30, 1982, we are projecting a volume of more than $100 million.
>
> Capitalization: The program is capitalized by the sale of tax-exempt revenue bonds. The debt is the sole obligation of the Coordinating Board and is not backed by either the credit or taxing power of the State.
>
> Special Allowance Payments: Loans made under the Program prior to October 1, 1980 earn the full special allowance payments from the federal government, ensuring a variable yield equal to the bond equivalency rate on 91-day treasury bills plus 3.5 percent. Loans made after October 1, 1980 earn half this full special allowance payment, although in no case can the total yield (interest plus special allowance) fall below 9.5 percent.

Federal Arbitrage Restrictions: The Coordinating Board has covenanted to comply in all respects with the requirements of Section 103(c) of the Internal Revenue Code of 1954, as amended, and all applicable Department of Treasury regulations relating to arbitrage. By law, special allowance payments, however, are not considered interest earnings, for arbitrage purposes.

Use of Earnings: By statute and bond covenants any earnings derived from the operation of the Loan Program are dedicated to the costs of the Program or the acquisition of new loans.

The ultimate objective of the Coordinating Board in the financing of the Loan Program is to achieve balance in the following equation:

Loan Repayments + Reserves + Earnings = Debt Principal and Interest Payments + Operational Costs

Sallie Mae's Role With Respect to Statewide Tax-Exempt Lenders

Given the volatility of the national economy and its reflection in the tax-exempt bond market, it has been difficult for some time to assure a balance between revenues and expenses. These circumstances have nearly closed off access to long-term definitive financing (matching loan and debt repayments) for student loan programs. Thus the financing of student loan programs for the past three years has been primarily dependent on the short-term market, increasing the risks, costs and complexity of each issue.

In the short-term market (usually 3-5 years) the term of debt is considerably shorter than the potential repayment schedule assured borrowers by federal law (10 years + deferments + in-school period). Thus to assure bond purchasers that their capital can be repaid on schedule, some device for ensuring intermediate liquidity has been expected by the rating agencies and potential purchasers. The devices most frequently used in the past three years have been forward purchase commitments by banks or Sallie Mae and letters of credit from major national banks. Letters of credit generally result in higher bond ratings, however, the continuing costs to the issuer are also greater, thus offsetting the lower interest rates that accompany higher bond ratings. The costs of these intermediate devices vary with other market rates and are sufficiently high to be a factor in financial feasibility for smaller and immature issuers. Another factor, which has been increasing in frequency, is the expectation that the issuer will designate the provider of the credit assistance as a senior manager in the underwriting of the bond sale. This arrangement is both costly (up to 3% of the total bond value) and limiting since it precludes the competitive sale of the bonds.

From about 1976 to 1979, Sallie Mae was generally meeting the needs of a number of statewide lenders through forward purchase commitments. These agreements provided needed security, financing flexibility, and were instrumental in assisting a number of states in meeting additional student loan demands. The specific terms of the agreements varied significantly and all were the result of lengthy and technical negotiations. In many instances Sallie

Mae guaranteed par purchases for notes of in-school or grace status and a reasonable discounted price for loans already in repayment. For many newer programs the Sallie Mae commitment agreement was the only vehicle available to assure success with the rating agencies and the marketplace. Through these arrangements Sallie Mae helped establish appropriate standards relating to the origination and servicing of these loans.

Specific Problems We Face In Working With Sallie Mae

The problems in working with Sallie Mae fall generally into two categories:

- Sallie Mae's failure to work out agreements in a timely fashion.
- Sallie Mae's failure to offer reasonable competitive terms in agreements with state lenders.

Sallie Mae's Failure to Work Out Agreements in a Timely Fashion

A perennial major limitation in working with Sallie Mae has been the organization's inability or unwillingness to work out agreements on a timely basis. For example, in 1981 we discussed a commitment agreement with Sallie Mae but were unable to secure a complete negotiated package prior to the bond sale for which the commitment was needed. Recently, these problems have continued. On February 12, 1982 we requested a proposal from SLMA that would supply additional security to our planned revenue bond issue. The only criteria for the proposal was that the proposed security for our bonds would adhere to our currently outstanding bond resolutions. As of this date, six weeks later, we have not yet received a proposal. We have initiated two verbal discussions regarding this, in which SLMA indicated interest but would not state when or whether such a proposal would be forthcoming. When such a request was submitted to other entities, we normally received proposals within three weeks.

Whether by design or in effect, Sallie Mae's delays have often left tax-exempt lenders, such as ourselves, in the untenable position of having to accept their conditions at the last moment, search for an alternative source of support on short notice, or simply not provide loans. For a mature program, such as Minnesota's, alternatives to Sallie Mae have been available in recent years. But for neophyte state programs that lack reserves and a proven record, Sallie Mae is often the only alternative. And even for mature programs Sallie Mae remains an important resource because it is not clear that other alternatives will continue to remain available in the future.

Sallie Mae's Failure to Offer Reasonable/Competitive Terms in Agreements with State Lenders

At some point in 1979 or early 1980 Sallie Mae's terms for entering into forward commitments changed dramatically, suggesting that the organization's concern and appreciation for statewide loan programs has diminished. Although Sallie Mae did not publicly announce a change in policy, the integral features of contracts changed in two important ways.

First, Sallie Mae's proposed terms have shifted virtually all real or potential risk in the prospective arrangement to statewide programs. For example, in 1980, Sallie Mae proposed as a condition that the Minnesota program, as the future seller of loans, agree to pay any servicing costs in excess of 1.5 percent over the entire life of loans in order to avoid prohibitive discounts. When my colleagues and I have complained that such changes would be incompatible with either the actual costs of servicing loans or with the yields provided on tax-exempt student loans, Sallie Mae has been less than responsive. Invariably, Sallie Mae's suggested remedies are either not allowable within current legal restrictions or they are simply financially infeasible.

Second, Sallie Mae has proposed terms that would significantly increase its potential profits from commitment agreements. For example, Sallie Mae has offered only to purchase notes of in-school or grace status. Furthermore, Sallie Mae has continued to demand larger average consolidated loan amounts. For instance, Sallie Mae has indicated that under present terms in the Minnesota program we would need an average consolidated loan size of more than $5,000 to be assured of par sales with them. The net effect of this requirement would be either to force lenders to encourage students to take out larger and multiple loans to achieve the highest purchase price possible in Sallie Mae's pricing grid, or to accept commitment agreements that increase the state program's financial liability. Encouraging excessive borrowing clearly is not an option for statewide lenders - it is contrary to state policy, not in the students' best interest, and ultimately more costly to the federal government.

Effects of Problems State Lenders Face with Sallie Mae

In combination, these problems discussed above have in many instances changed a Sallie Mae forward commitment agreement from an asset to a financial liability for our programs. In our judgment, Sallie Mae currently does not provide a service that meets the needs of statewide lenders.

Because the Minnesota program is rapidly approaching financial maturity and has a proven record in the bond market, we have had the luxury of finding better terms elsewhere, and thus are in a position from which we can criticize Sallie Mae's performance. The irony of this situation is worth emphasis. Our program has been able to secure better overall terms from private banks, which have not had the benefits of federal subsidies and access to the Federal Financing Bank. And Sallie Mae's apparent disinterest in serving statewide lenders has occurred at the same time that Sallie Mae's profits have grown dramatically. In 1980, while Sallie Mae negotiators were offering 95 percent on notes that previously would have been accepted at par, their earnings increased by nearly 50 percent (from $6.4 million in 1979 to $9.4 million in 1980).

The evidence provided above suggests that a subtle transition in Sallie Mae policy has indeed occurred. It appears that the current Corporation is more concerned with maximizing profits than with serving a diverse clientele. And there is little reason to believe this implicit policy will change. I believe that four factors will continue to provide impediments to successful negotiations between statewide lenders and Sallie Mae:

1. Sallie Mae's transition to the private markets for capital will mean that its periods of greatest hesitancy and self-protecting behavior will occur at precisely the same times that statewide programs capitalized through the tax-exempt market will need assistance and protection;

2. Sallie Mae's recently acquired direct lending authority (as a lender of last resort) conflicts directly with its role as a secondary market for other lenders of last resort.

3. Sallie Mae's staff and Board have no external policy guidance to direct their decisions relating to the competing objectives of assisting clients (risks and liabilities) or maximizing profits (assets and comfort); and

4. There is no continuing mechanism to review Sallie Mae's performance or leverage for inducing desired behavior.

The magnitude of this situation should not be overlooked. The statewide programs are currently serving the loan needs of more than 20% of the national volume. If for any reason the participation of banks or savings and loans should decrease in the next few years, the dependence on the statewide programs will increase. If the pattern of reductions in other federal and state financial aid programs should continue, the increased loan volume which results will, in many states, be borne by statewide programs capitalized by tax-exempt borrowing. If we are to continue to meet these needs and meet the requirements imposed by the marketplace, we will need effective, dependable, and affordable services from a national secondary market dedicated to serving student loan needs. We cannot depend upon the commercial sector to meet the major portion of these needs because of competing demands on their capital resources. On the other hand Sallie Mae's sole purpose is to assist in the maintenance of student loan credit and I believe that this mandate ought to require that Sallie Mae provide a dependable and affordable secondary market for statewide programs.

I appreciate your interest and hope the Committee will continue to take an active interest in the appropriate roles and performance of Sallie Mae.

Sincerely,

Clyde R. Ingle

CLYDE R. INGLE
Executive Director

cc: Members of the Committee
Minnesota Delegation

REAGAN ADMINISTRATION'S PROPOSAL TO ELIMINATE GRADUATE/PROFESSIONAL STUDENTS FROM THE GUARANTEED STUDENT LOAN PROGRAM

IMPACT AT UNMC

BACKGROUND INFORMATION

The enclosed chart depicts statistical data for the 1981-82 school year. At UNMC, 965 graduate/professional students processed guaranteed student loan applications totaling $4,181,200. This represents 72.1% of the graduate/professional enrollment and 69.4% of total financial aid of $6,022,748 received by 1,061 graduate/ professional students.

Of the 965 GSL recipients only 357 or 37% can be identified as having financial need as determined by a formal need analysis. These students received GSL's totaling $1,423,300 or 34% of total GSL's received by all graduate/professional students.

Since guaranteed student loans for 1981-82 could be obtained on a "no need" basis with no requirement to disclose financial information, the real needs of 608 students cannot be determined. However, it is recognized that a percent of these students do in fact have need, but opted to use GSL to meet that need rather than apply for the more restricted "need based" aid programs.

In November 1978 the U.S. Congress made the GSL a "no need" loan program. Prior to this major change, the program operated under a "need test" based on a family income cap. Following is a comparative study of the percent of GSL recipients before and after November 1978.

3) The ultimate independent decisions of students and/or families to pursue the expensive alternative of high interest loans. This is the most important factor for which estimates or assumptions are difficult to make.

While it is quite easy to assess the impact of lost dollars and the probable use of alternatives, it is extremely difficult, if not impossible, to make judgements on the numbers of students who may have to terminate their studies next year or reduce their studies. The students most likely to terminate or reduce studies can be placed into three general catagories.

1) Single students with dependents to support.
2) Married students with children whose spouses cannot contribute to the financial resources.
3) Other students with unusual financial circumstances.

The implications at UNMC must be assessed by educational discipline since there are variables amongst the programs. Following are impact statements by discipline for the numbers of students for whom there is immediate concern. It is assumed that all other students will avail themselves to other resources as the students did before November 1978.

GRADUATES (60 Students)

In 1981-82 only 6 of the 76 GSL recipients demonstrated financial need. Considering potential reductions in fellowships and traineeships it is anticipated that several more will show need in 1982-83.

It is estimated that at least 20 students would depend upon the full amount of $5,000 GSL in 1982-83. The remaining 40 would depend on an average amount of about $3,000 GSL to supplement other resources.

It is felt that half of these students would be far enough into their graduate studies that they would be willing to borrow higher interest loans to complete their program if no GSL loans.

	1977-78	1981-82
DENTISTRY	43.0% (Est.)	87.4%
MEDICINE	43.8%	81.9%
PHARMACY	17.8%	75.7%
GRADUATES	9.8%	29.9%

These data indicate that fewer students need and depend upon guaranteed student loans than those receiving them. Clearly, the impact of the proposed change to eliminate graduate/professional students from the program must be focused on those students who can demonstrate some degree of financial need.

Using 1981-82 data for those students who demonstrated need by a formal need analysis, estimating a percent of other students who probably could have demonstrated need, and other data, the numbers of graduate/professional students for whom there is most concern for 1982-83 are estimated as follows.

	NO.	EST. % OF ENROLLMENT
DENTISTRY	125	50%
MEDICINE	300	50%
PHARMACY	85	40%
GRADUATES	60	25%
	570	43%

IMPLICATIONS - NO GUARANTEED STUDENT LOAN FOR 1982-83

The impact of the loss of guaranteed student loans to graduate/professional students is extremely difficult to assess for several reasons. The three most important are listed below.

1) The lack of information to be able to determine potential resources and "real need" for all students.
2) The lack of information and uncertainty of the final outcome of funding levels in all other programs that are available to assist students.

The remaining half would perhaps first consider reducing their gram, secondly consider higher interest loans, or finally, decide o discontinue studies.

Assuming ALAS loans (Auxilary Loans to Assist Students) at 14% interest will in fact be available, and with some support from our donated loan funds, perhaps no student would drop out.

In the event ALAS loans are not available, which is indeed a possibility, then perhaps 20 students would have to consider dropping out.

DENTISTRY (125 Students)

Approximately 85 students will demonstrate need and will qualify for GSL and other need based aid. Since there will be some reductions in the need based aid these students would all need the $5,000 maximum amount of GSL. The other 40 students, not eligible for need based aid, would need an average of $3,500 GSL each.

If the GSL were not available, all need based aid would be directed to the most needy, about 50 students. It is expected that at least for 1982-83, we will be able to fund these students.

The remaining 75 students would have to resort to either the ALAS loan at 14% interest or the HEAL loan (Health Education Assistance Loans) at 16% to 18% interest, or a combination of these two loan programs.

If all dental students had access to ALAS and HEAL loans and were willing to accept the high interest rates, they all could stay in school. If ALAS loans are not available, but HEAL loans are, they still could stay in school. In both cases the loan debts will increase considerably.

If neither are available or funds are in limited supply, perhaps 30 students would have to consider leaving school.

MEDICINE (300 Students)

Approximately 200 students will demonstrate need and will qualify for GSL and other need based aid for 1982-83. Considering the almost certain reductions in need based aid, these students would all need the $5,000 maximum amount of GSL. The other 100 students, not eligible for need based aid, would need an average of $3,500 GSL each.

If GSL were not available, all need based aid would be directed to the most needy, about 100 students. It is expected that there will be adequate federal and institutional aid to fund these 100 students for 1982-83.

The remaining 200 students would have to resort to either the ALAS loan at 14% interest or the HEAL loan at 16% to 18% interest, or a combination of these two programs.

Assuming the students will have access to ALAS and HEAL loans and would be willing to borrow at the high interest rates, they all could stay in school. If ALAS loans are not available, but HEAL loans are, they could still remain in school. In both cases the loan debts will increase considerably.

If neither alternative is available or funds are limited in supply, perhaps 30 or more students would have to consider leaving school.

PHARMACY (85 Students)

Pharmacy students are in a unique situation. At times they are classified as professional students and at other times classified as undergraduates depending upon which aid program is being considered. This situation exists because of conflicting federal rules and regulations for defining graduate/professional and undergraduate students for the various federal aid programs. The professional classification used for this study.

Approximately 60 students will demonstrate need and will qualify for GSL and other need based aid for 1982-83. Like Dentistry and Medicine, there will be reductions in need based aid for Pharmacy. These students will need an average of $3,000 GSL each. The other 25 students, not eligible for need based aid, would need an average of $2,000 GSL each.

If GSL were not available, all need based aid would be directed to the most needy, about 40 students, who could be funded for at least 1982-83 with federal and institutional funds.

The remaining 45 students would have to resort to either the ALAS loan at 14% interest (if eligible as a graduate/professional) or the HEAL loan at 16% to 18% interest, or a combination of these two programs. Pharmacy students are eligible for the HEAL loan program.

Like dental and medical students, these students could stay in school assuming there will be access to either the ALAS or HEAL loans and students were willing to borrow at the high interest rates which will increase their indebtedness.

If neither alternative is available or funds are limited in supply, perhaps 20 or more students would have to consider leaving school.

SUMMARY OF IMPACT

This study was made assuming that those students (over 750) who do not demonstrate financial need through a formal need analysis will avail themselves to other financial resources if the GSL program is discontinued. These other resources would be families, spouses, other relatives, private sources, higher interest loans, or a combination of those potential resources. It is believed that these students will not have to consider leaving school.

proximately 570 students or about 43% of the anticipated 83 enrollment would be dependent upon some GSL support. Of se, 365 will show need and will be dependent upon the more restrict- d need based aid funds. The other 205 students would be dependent pon GSL only since they would demonstrate some need, but not great enough to be eligible for the need based funds.

If the GSL program is terminated, the need based funds will have to be directed to the "neediest of the needy" in which case only 200 needy students could be funded for 1982-83. These students would be from the lowest family income backgrounds.

If only 200 students could be funded with need based aid, 370 students would have to turn to the high interest ALAS and HEAL loan programs. At present, there is very much doubt nationally that the ALAS program will be available since lenders are reluctant to participate. The outlook for the HEAL loan program is not much better.

If ALAS and HEAL loans will in fact be available and assuming students would borrow at the higher interest rates, it is believed that currently enrolled students would remain in school. There is much more uncertainty about entering students who would be looking at much higher indebtedness.

Assuming the worst of circumstances with no GSL, no ALAS, no HEAL, and reduced funding in other programs, perhaps 100 or more graduate/professional students would have to consider terminating their studies in 1982-83 and perhaps more in future years. The numbers by educational program are as follows:

DENTISTRY	-	30	PHARMACY	-	20
MEDICINE	-	30	GRADUATE	-	20

The affects, it is believed, will be much greater in the future as students in the pipeline are able to assess the implications.

UNIVERSITY OF NEBRASKA MEDICAL CENTER

DUCATIONAL PROGRAM	ENROLLMENT FALL 1981 F.T.	P.T.	TOTAL ENROLL.	GUARANTEED STUDENT LOAN RECIPIENTS (1981-82) GRAD/PROF. STUDENTS — FULL-TIME NO.	AMOUNT	% OF ENROLL.	PART-TIME NO.	AMOUNT	% OF ENROLL.	TOTAL NO.	AMOUNT	% OF ENROLL.
ROFESSIONAL												
DENTISTRY	261	-0-	261	228	$1,091,400	87.4%	-0-	$ -0-	-0-	228	$1,091,400	87.4%
MEDICINE	609	4	613	499	2,279,900	81.4%	3	13,500	.5%	502	2,293,400	81.9%
PHARMACY	208	2	210	157	451,500	74.8%	2	6,000	.9%	159	457,500	75.7%
OTAL PROF.	1,078	6	1,084	884	$3,822,800	81.5%	5	$19,500	.5%	889	$3,842,300	82.0%
RADUATE												
DENTISTRY	21	7	28	17	$ 85,000	60.7%	-0-	$ -0-	-0-	17	$ 85,000	60.7%
MEDICINE	47	48	95	19	85,400	20.0%	5	25,000	5.3%	24	110,400	25.3%
NURSING	48	49	97	20	82,700	20.6%	8	37,600	8.3%	28	120,300	28.9%
PHARMACY	20	14	34	7	23,200	20.5%	-0-	-0-	-0-	7	23,200	20.5%
TOTAL GRAD.	136	118	254	63	$ 276,300	24.8%	13	$62,600	5.1%	76	$ 338,900	29.9%
TOTAL GRAD/ PROF.	1,214	124	1,338	947	$4,099,100	70.7%	18	$82,100	1.4%	965	$4,181,200	72.1%

PREPARED BY: OFFICE OF FINANCIAL AID
2/4/82

University
of Nebraska
Medical Center

Office of Financial Aid
42nd and Dewey Avenue
Omaha, NE 68105
(402) 559-4199

MEMORANDUM

TO: Dr. N. A. Vanselow, Chancellor

FROM: Bob Fredlund, Financial Aid B.F.

DATE: February 22, 1982

RE: Impact Study - Funding Cuts and Program Changes for Federal Student Financial Aid

The enclosed study is an initial assessment of the impact at UNMC resulting from recent and proposed funding cuts and program changes to federally sponsored student aid programs.

As we discussed on February 8th, UNMC students in all academic programs will be impacted so this study includes all programs. Hopefully, the enclosed comments and statistical data will give you and the Medical Center Administration a clearer understanding of the situation.

After you have had an opportunity to review the information, I would appreciate an opportunity to visit with you.

Encl.

CC: John E. Aronson

RECEIVED
UNIVERSITY OF NEBRASKA
FEB 22 '82
U of Nebraska Medical Center
Office of the Chancellor

PREPARED BY: Robert T. Fredlund, Director of Financial Aid, U. of N. Medical Center
ASSISTED BY: Office of Financial Aid Staff, U. of N. Medical Center
PREPARED FOR: Neal A. Vanselow, M.D., Chancellor, U. of N. Medical Center
DATE: February 22, 1982

IMPACT STUDY OF FINANCIAL AID PROGRAMS RESULTING FROM:

1. FEDERAL LEGISLATIVE CHANGES - 1981
2. FEDERAL FISCAL YEAR 1982 FUNDING LEVELS (TENTATIVE)
3. REAGAN ADMINISTRATION'S PROPOSED FY 1983 BUDGET
4. REAGAN ADMINISTRATION'S PROPOSED LEGISLATIVE CHANGES TO GUARANTEED STUDENT LOAN PROGRAM

BACKGROUND INFORMATION

The Reagan Administration's Budget Reform Plan of 1981 resulted in the passage of two pieces of legislation with each having significant affects on student assistance. First, the Omnibus Budget Reconciliation Act of 1981 (PL 97-35) was passed on August 13, 1981. Secondly, the Joint Continuing Resolution (PL 97-92) was passed on December 15, 1981. These bills made numerous changes to financial aid programs and dramatic reductions in funding levels. These bills followed FY '81 funding adjustment legislation wherein some funds were reduced for the 1981-82 school year.

All of the 1981 legislation had some affect on the aid programs for 1981-82, but the real impact will be felt in 1982-83 and beyond. The impact on students for 1981-82 was not significant. However, in 1981-82 a few students lost eligibility for some aid, several were assessed fees, and others will be assessed with higher interest rates on a portion of their student loans.

The 1981 changes and funding levels (tentative) coupled with the Reagan Administration's proposed FY 1983 budget and changes to the Guaranteed Student Loan Program seemingly indicate a disaster for UNMC's financial aid program. The magnitude of both program changes and funding cuts are extremely alarming. The recent and proposed program changes and funding reductions are summarized in Enclosure #1.

IMPACT

The impact at UNMC upon its students in terms of dollars alone is very significant. Moreover, the impact could extend to such areas as admissions, retention, curriculum structure, career counseling, debt management, and possibly other areas. Further, the impact will extend beyond UNMC and its students. Clearly, the families of students (parents) and students' families (dependents) will be affected. And last but not least, there will be an impact to the lending community since there is significant dependency upon that sector.

The broad range of all possible areas which could be impacted is obviously beyond the evaluation capabilities of the Office of Financial Aid. Therefore, the scope of this study is directed to the financial impact on student aid. Further, this study is directed primarily to the "need based" aid programs and to that portion of the student body for whom it can be determined there is "real need" through a formal need analysis. These students are the recipients of need based aid. Included are some estimates for another portion of the student body for whom there is no documented need, but it is believed some need exists. Finally, the remaining students are considered not needy and the impact would be negligible if any.

Enclosure #2 shows the projected losses of new federal capital for the various federal need based aid programs while Enclosure #3 shows the projected decline of total available dollars for these same programs. The latter figures include new capital, matching funds, cash balances, and loan repayments.

Enclosure #4 with explanatory comments is a three year projection of the students who are considered to be the most "needy". The data depicts the need analysis and aid resources available to meet needs. The recent and proposed funding cuts and program eligibility changes were applied to these projections. It is the "needy" students and their families who will feel the greatest impact. However, other students and families will also feel the impact.

Thusfar, the data and comments have reflected on the impact in general. Unfortunately, the precise impact on individuals which is most important cannot be portrayed in this study since each individual will be affected differently as will individual families. Similarly, the educational programs will be impacted differently.

At this point, it seems appropriate to make some assessment of the impact upon families. The need analysis data (Encl. #4) reflect estimated family and student contributions. The estimate of need assumes these contributions to be available at 100% regardless of student dependency status. While it is likely most student or student and spouse contributions will be available, it is not likely that all expected family (parental) contributions will be. Some parents will contribute while others will not or cannot. The expected parental contribution is estimated to be about 38% of total family and student contribution. Applying that ratio to the 1982-83 data, the expected parental help would be near $1,000,000. Previously, the Guaranteed Student Loan (GSL) program allowed students to borrow the parental contribution at least up to the amount of the GSL. The Reagan proposals will eliminate that practice. The alternatives for parents are limited in terms of student aid programs. In the case of graduate/professional students, the students would have to borrow at 14% or at the "market rate" of interest under the Auxiliary Loan to Assist Students (ALAS) or Health Education Assistance Loan (HEAL) programs respectively or a combination of those loans. Parents cannot borrow from any aid program. Dependent undergraduate students' parents would have to borrow at 14% under the Parents Loan for Undergraduate Students (PLUS) if they were not able or choose not to contribute. The amount of borrowing in both situations will be tempered by individual student and family decisions, thus the potential loan demand is unpredictable. More important is the alarming concern locally and nationally that these loan resources may not be available. The lending community, it is believed, is not receptive and is moving very cautiously. Obviously, the impact on students and families is significant in terms of resolving the matter of contributing or being forced to borrow at high interest.

The analysis for 1982-83 reflects a deficit (unmet need) in excess of 1.5 million dollars. The projected resources did not take into account the PLUS/ALAS or the HEAL loan programs since these are essentially "no need" programs. The purpose of the analysis format is to illustrate the impact of the Reagan proposals and the deliberate intentions to force students and parents to borrow from the higher interest loan programs. The data reflects the potential need for such loans which may not be available.

As indicated earlier, the educational programs are impacted differently. Following are some of the implications.

Students in the three health professions programs, it appears, will all need access to the ALAS and HEAL loans. While the data indicates the "need based" aid resources would be adequate to fund about 50% of the needy students, this will not happen. Funds restrictions such as annual amounts, other criteria, and limited funds will prohibit funding any one student at 100% with few exceptions. Thus, all will need ALAS and HEAL loans or a combination, but in varying amounts. This would be in addition to loans needed for parental help that may not be there. Consequently, even the "neediest of the needy" will be forced to access the high interest loan programs. Assuming availability, the net result will be larger loan debts and complicated loan repayment portfolios which obviously have other implications. The real impact will of course be felt by those students with the longest time remaining until completion of their education at UNMC and those in the pipeline. The data indicates the problem is potentially more serious in pharmacy than medicine and dentistry.

The impact upon graduate students is more difficult to assess since information is not available on such resources as assistantships, fellowships, and traineeships. These resources, it is believed, are also declining. The choice for graduates is limited. Very little need based funds would be available and the only other loan alternative would be the high interest ALAS loan.

The impact upon Allied Health students will be quite severe. The unmet need in 1981-82 is an indication that the costs are already greater than the available resources. Student aid program constraints (loan limits, etc.) have in many cases prevented full funding. This situation will become more severe in the future. Further, the alternatives are very limited. Independent students (a large number) will be able to borrow only a maximum amount of $2500 less origination and other fees from either or a combination of the GSL and ALAS programs. The projected shortage of need based aid and the loan limit constraint will result in large shortfalls for many students. Dependent students have little alternative except for parents borrowing under the PLUS program. The 1982-83 and 1983-84 projections assume maximum borrowing under GSL in addition to other aid, yet the unmet amounts of need are significant. It is evident that students with limited resources will probably not be able to pursue those Allied Health programs with high costs. For those who may have some resources and who would have to borrow the maximum GSL on to, or other loans, the increased debt obligation will be significant. The proposal to assess "market rate" interest on GSL starting two years after leaving school on top of the total loan debts of students would be devastating. The potential impact in all areas for the Allied Health program is believed to be serious.

The undergraduate nursing programs which appear to be the least affected dollar-wise will be impacted like Allied Health students. Students in the A.S. program will be impacted the greatest. Students in the B.S. program typically have lesser needs since there is considerable self-help through work. Those students with limited resources and those with unusual needs will find it very difficult to enter or remain in school. Like Allied Health, the projections of available funds for nursing assumes maximum borrowing under the GSL program. The potential increased debt obligations would be a serious consequence.

In addition to the students for whom we have or will have documented need, there is a significant number of students who have need but usually not sufficient to qualify for need based aid. These students (numbers and need unknown) have accessed the GSL program. It is estimated that 250 graduate/professional students may fall in this category. Since they do not qualify for need based aid and would no longer be eligible for GSL, they would have to resort to the ALAS/HEAL loans to the extent that family resources would not be available. It is estimated these students would need support for at least tuition, fees, books, etc. Assuming an average loan of $3,000, the demand could be about $750,000 for loan funds that may not be available. The impact here would not be as significant assuming the alternative loan resources will be available.

It is estimated that 150 or more undergraduate students have similar circumstances in terms of need. There is no alternative student loan program for those students who claim independence. The alternative for dependent students is the PLUS loan for parents. Assuming parents and students contributed the maximum possible amounts of self-help and there is remaining need, more demand for funds would be placed on the PLUS program. If parents were forced to borrow at the same level as they have borrowed under GSL ($2500), the demand could reach $250,000 for PLUS loans.

Assuming the Reagan Administration is successful and pending further study, there is an immediate need to obtain some form of response from the lending community in Nebraska. The potential demand for PLUS/ALAS and HEAL loans could exceed 2.5 million in 1982-83 and much more in 1983-84. Considering the potential non-availability of these resources, any recommendations or resolutions as to financing students in 1982-83 and beyond would be unwise. The University should not get into a position wherein these loans are recommended as alternative resources when in fact they may not be available. If the PLUS/ALAS and HEAL programs are to provide a "safety net", then it appears the strength of the net must be known before relying on it.

In summary, the combined funding cuts and program changes could have a devastating impact on UNMC students and families. Obviously, there is need for further study and analysis of the total impact. Also, there is a pressing need to prepare a coordinated response to the total impact. In this regard, it seems appropriate that key faculty, staff, and students meet to further study the impact and formulate a unified position.

ENCLOSURE #4

UNMC APPLICANTS FOR NEED BASED AID

EXPLANATORY COMMENTS

These data concern only students with documented financial need.

1981-82 data reflect actual experience as of 2-1-82.

1982-83 and 1983-84 data reflect best estimates. Since costs, contribution and need are very unpredictable, these data were kept constant in 1983-84 for purposes of this study.

Aid received by students in 1981-82 in excess of need except for Allied Health is largely a result of students borrowing under Guaranteed Student Loan program as an offset to parental contribution.

The unmet need in Allied Health involves several students with unusual needs who received maximum possible federal aid.

Projected federal aid resources for 1982-83 and 1983-84 reflect funding cuts and program changes.

All estimated available school (donated) loan funds are projected to be expended in 1982-83. Only limited loan repayment funds would be available in 1983-84 and beyond.

Other aid resources are expected to decline as greater numbers of students pursue this alternative.

The Family/Student Contribution assumes 100% of expected contribution regardless of students' dependency status with parents.

Excluded from any projected resources are:

1) the Parents Loan for Undergraduate Students/Auxilary Loan to Assist Students (PLUS/ALAS) programs and 2) the Health Education Assistance Loan (HEAL) program.

The purpose in excluding these programs is to illustrate the impact of lost funds and program changes which will force students and parents to turn to higher interest loans which may not be available.

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FEDERAL NEED BASED FINANCIAL AID PROGRAMS
FUNDING LEVELS (NEW CAPTIAL) FOR UNMC

AID PROGRAM	1981-82		1982-83		1983-84
HEALTH AND HUMAN SERVICES PROGRAMS					
HEALTH PROFESSIONS LOANS					
DENTISTRY	$ 27,900	Est. 65% cut for 1982-83	$ 9,765	No budget for 1983-8	$ -0-
MEDICINE	82,137		28,750		-0-
PHARMACY	27,252		9,538		-0-
NURSING LOANS		Est. 50% cut for 1981-82. These funds not yet received.		No budget for 1982-83 nor 1983-8	
ASSOCIATE DEGREE	11,408		-0-		-0-
BACCALAUREATE DEGREE	2,500		-0-		-0-
MASTERS DEGREE	1,995		-0-		-0-
EXCEPTIONAL FINANCIAL NEED SCHOL.		Est. 50% cut for 1982-83		No budget for 1983-8	
DENTISTRY	46,487		23,243		-0-
MEDICINE	29,178		14,589		-0-
DEPARTMENT OF EDUCATION PROGRAMS					
PELL GRANT	227,489	Est. 10% cut for 1982-83	204,741	Est. 40% cut for 1983-84	136,000
SUPPLEMENTAL GRANT	37,940	Est. 25% cut for 1982-83	28,470	No budget for 1983-8	-0-
INCENTIVE GRANT	6,440	Program transfers to State control for 982-83. No dollars budgeted for 1983-84.			----
NATIONAL DIRECT LOAN	138,103	Est. 4% cut for 1982-83	132,579	No budget for 1983-8	-0-
COLLEGE WORK STUDY	35,000	Est. 4% cut for 1982-83	33,500	Est. 30% cut for 1983-84	24,000
TOTAL	$673,829		$485,175		$160,000
% OF REDUCTION FROM 1981-82	----		28%		76%

ENCLOSURE #2

FEDERAL NEED BASED FINANCIAL AID PROGRAMS

PROJECTED AVAILABLE FUNDS (CASH BALANCES, NEW CAPITAL, MATCHING FUNDS, LOAN REPAYMENTS)

AID PROGRAM	1981-82		1982-83		1983-84
HEALTH AND HUMAN SERVICES PROGRAMS					
HEALTH PROFESSIONS LOANS					
DENTISTRY	$ 408,000		$ 290,000	Loan repayments only after 1982-8	$127,000
MEDICINE	415,000		342,000		235,000
PHARMACY	75,000		58,000		39,000
NURSING LOANS					
ASSOCIATE DEGREE	66,000	Late 81-82 funding to be carried over to 1982-83	27,000	Loan repayments only after 1981-8	20,000
BACCALAUREATE DEGREE	34,000		35,000		15,000
MASTERS DEGREE	9,200		7,700		1,000
EXCEPTIONAL FINANCIAL NEED SCHOL.					
DENTISTRY	46,487		23,243		-0-
MEDICINE	29,178		14,589		-0-
DEPARTMENT OF EDUCATION PROGRAMS					
PELL GRANT	227,489		204,741		136,000
SUPPLEMENTAL GRANT	37,940		28,470		-0-
INCENTIVE GRANT	6,440	Program transfers to State control for 1 82-83. No dollars budgeted for 1983-84.			---
NATIONAL DIRECT LOAN	242,000		235,000	Repayments only after 1982- 3	75,000
COLLEGE WORK STUDY	35,000		33,500		24,000
TOTAL	$1,631,734		$1,299,243		$672,000
% OF REDUCTION FROM 81-82	----		21%		59%

3/9/82

FACT SHEET

Financial Aid At The University of Nebraska Medical Center

1. In 1981-82, 965 graduate/professional students (medicine, dentistry, pharmacy, graduate college) took Guaranteed Student Loans totalling $4,181,200. This represents 72% of UNMC's graduate/professional enrollment and 69% of the total financial aid received by students in these categories.

2. The UNMC financial aid office estimates that 570 graduate/professional students, or 43% of the enrollment in these categories, have a demonstrable need for financial aid (since November 1978 the Guaranteed Student Loan Program has been on a "no need" basis). If graduate/professional students are no longer eligible for GSL's, programs other than Auxiliary Loans to Assist Students (ALAS) and Health Education Assistance Loans (HEAL) will not meet the demand for aid funds.

   a. In 1982-83 students will have to turn to ALAS and HEAL for over $1,500,000 of aid

   b. In 1983-84 students will have to turn to ALAS and HEAL for over $2,300,000 of aid

3. ALAS and HEAL have very unfavorable interest rates and are not currently available to all Nebraska students. Students who can get these loans will be faced with the spectre of repaying large sums of money after graduation.

4. If the Administration's proposal to make graduate/professional students ineligible for GSL's becomes law, we anticipate that at UNMC:

   a. As many as 100 students may be forced to drop out of school (30 medical students, 30 dental students, 20 pharmacy students, 20 graduate students).

   b. Some students will decide against a career in the health professions because of the size and type of debt they will incur. We believe students in the following categories will be particularly affected:

      1) minority students
      2) rural students
      3) married students with children
      4) other low income students

   c. Those students who are forced to take ALAS and HEAL loans may elect to enter high income specialties and practices rather than primary care specialties (such as family practice) where the need is the greatest.

5. Undergraduate students at UNMC (nursing and allied health) will also be adversely affected by proposed changes in the federal student loan program.

6. The default rate on loans made to students at UNMC is less than 2% -- one of the lowest rates in the United States.

Mr. **Ingle**. Now, I think I would also mention here that while we were not able to negotiate a commitment with Sallie Mae, we were able, as you mentioned, Mr. Erdahl, to get a commitment from two St. Paul commercial lenders which allowed us to stay in the business of providing loans.

We have no assurance whatsoever in the current market for funds that we will be able to do that in the future. So the critical question which I would like to call to your attention is how the Nation or the State, separately or in combination, will insure that credit is available for those students who need it.

It is perhaps not a major problem for those who do not need it, but in the course of the last year we have had tuition increases in Minnesota ranging from $100 to $400 in the private sector. Next fall the increase will be 30 percent over last fall in the public sector. At the same time, the assistance available to students is down both at the Federal and State level.

We feel very strongly that the triple pincher for students at the lower end of the economic scale is going to seriously threaten the long-held goals of promoting equal opportunity at the State and national level.

I want to make it clear here that the question that I think the committee, from viewing this from the perspective of the State, must address is what is available at the secondary market level which is reasonable.

If it is the intent to provide this kind of capital credit from the national level, then I concur with that. If it is not and there is an intent to continue to provide opportunities at the State level to meet the needs of State citizens, then the function of the secondary market has to be very closely paid attention to.

If there is going to be any kind of subsidy for those people who may not be able to afford the full burden of the cost of that debt, as Mr. Martin suggested earlier, then I think the committee must address that.

Mr. **Simon**. I guess I am not clear in my own mind whether your criticism is of Sallie Mae or in fact is of the national program that is evolving. When you talk about a technical problem, in response to Mr. Erdahl, are you talking about the price that they offer you or the fact that you do not have a guarantee from the State of Minnesota? Or is it not one of these things?

Mr. **Ingle**. Mr. Chairman, the technical problem ends up in a cost for the moneys which we have available to lend to students. That cost is a result of a number of factors, which I will spell out in writing to you. That is the precise problem that I think we have to deal with.

Now, we currently are lending in the State of Minnesota through this State authorized last resort program in the neighborhood of 50 percent of the student loans in the State.

If that is going to continue, we have to have this primary function of the secondary market taken care of. We have been concerned with the provisions in the law which were provided in the reconciliation bill which in our judgment open up a considerable amount of opportunity for other kinds of activities to compete with what we understood to be the primary purpose of providing a secondary market for student loans.

Again, the best example is if you are dependent upon a servicer and you find that servicer, the principal servicer, then becomes or has the opportunity to become a competitor, it is reasonably clear over a long period of time the terms for the service are going to be increased, may be increased, in order to become the primary operator. That is a concern we have.

Mr. SIMON. How many States do not guarantee, as Minnesota does now?

Mr. INGLE. Mr. Chairman, the case in Minnesota, we are not a guarantee agency. We are a direct lender. There is a guarantee agency that we relate to under the GSL, but we are not a guarantee agency.

I believe there are in the neighborhood of 26 to 29 direct lenders around the Nation. The exact number I do not know.

Mr. SIMON. Since Mr. Fox is still here, I am going to take the liberty to ask Mr. Fox if he would care to respond in any way here. I guess my question is, Is this a problem only in Minnesota? Is it a problem caused by the statute? I think those are the two first questions.

Mr. FOX. I would agree that it is a very complex issue. In response, I would say that as a creature of statute Sallie Mae has to uphold the highest standards of origination, servicing and collection and due diligence because we are going to be held to that standard by the Department of Education and also because we feel it is our role to try to have a sense of responsibility to those with whom we do business.

We cannot be anything less than what the statute requires in terms of collection, but with the constant changes that are undertaken and which require changes in systems, the cost of collections are very dear.

The fact that the program changes every year means that computer systems have to be changed. It means that the complex routines for dealing with the student have to change, and there is high cost associated with that.

Part of what is being talked about here is the high cost of collection. We deal with about 15 different State entities and provide a great deal of credit. We provide more credit and commitments to the State of Minnesota than any other State in the country.

We currently have a $200 million commitment outstanding against which the State agency can deliver loans. We provide perhaps twice as much in the way of commitments to this State than any other State with whom we deal, and we have done so at some risk to ourselves.

The profitability of our corporation is very nominal when you look at the total income of the State entities. They are making considerably more money than we have been with a much smaller commitment to a portfolio of student loans.

The question is one of risk, how far out do you want to go with any one institution over a period of time, and who is going to take the risk in terms of program change, collection cost change, interest rate change and the like.

While we are prepared to discuss and negotiate terms and conditions with anybody, the fact that we have $200 million worth of unused commitment outstanding to a State suggests to us that we have made an accommodation.

In addition, we have a $100 million commitment to a savings institution on a long-term basis in the State. Far and away the largest commitment we have to any State is in Minnesota. We are not prepared to deal with any State whereby the other 49 are subsidizing it. We have to deal fairly and consistently with every State.

I believe if you look at our profit statement you will find we are not making any irresponsible profits. As a matter of fact, we are making considerably less per unit of business than banking institutions make. We have to deal on a one-to-one basis and try to offer the services we can.

Mr. SIMON. I don't want to precipitate a debate here on the witness stand. One other question; that is, are you experiencing similar difficulties in other States.

Mr. FOX. In different types of States we have different types of problems. One is that there is not servicing capacity or servicing arrangements in place that certain States have arranged, and we cannot take the risk of undertaking to buy loans unless there is some assurance that if those loans come to us, they can be properly and appropriately collected.

So, we are working with many States in trying to develop servicing capacity.

Another problem is there is a tendency to issue very, very short-term notes in the revenue bond markets. Since the payout on a student loan can be 12, 13, or 15 years, financing 2- or 3-year bonds is an assurance there is going to have to be refinancing risk, that maybe we are going to have to undertake the purchase of these loans in the short term.

We may not have the resources ourselves, given the fact that we are changing the way in which we do business by administration consensus that we should be a private institution financing without the full faith and credit.

There are a lot of risks implicit in this. The question is, who undertakes the risks. With our organization having a very high debt-to-equity ratio and limited access to capital markets, there is a limit to how much risk we can take.

I don't even want to guess what this program is going to look like 2 or 3 years out, let alone in 1991. We have a commitment with the State of Minnesota that goes out to 1991, as it stands.

I don't believe Minnesota is not a well-meaning group or we are not looking at it in a well-meaning way. It is just the risks inherent in an environment of change do create problems for States.

If we do lend directly to Minnesota, it would be far easier than for them who have to take the risk of looking at the bond markets year after year. Yet, that option has been denied us by the department, even though this committee and the Senate feel they cured that problem in our statute or that inability of ours to provide service before.

Mr. SIMON. Mr. Weiss?

Mr. WEISS. Thank you, Mr. Chairman.

A lot of this I sense really is a problem of perception as much as anything else. Dr. Ingle has suggested in his testimony that he perceives the problem to be that you are no longer fulfilling the primary purpose for which you were created, or potentially you might not be because of the statutory authority provided you last year.

My question is, What is your response to that perception?

Mr. Fox. I think that a careful reading of the statute points out we cannot deal unilaterally in changing how we do business.

For example, it was alluded to the fact we might become a lender. We can only lend if there is a geographic shortfall and if the Secretary invites us in. We cannot become an insurer of student loans unless there is no facility in the State to do it on an equitable basis.

Again, we are invited in by the Secretary making a judgment. Unilaterally we cannot do any of those things. These things were put in last summer when there was the perception that the final law relative to student loans might be so restrictive of eligibility or might inhibit certain participants in the program that there might conceivably be a need for a broader responsibility for Sallie Mae.

That has come about to a modest extent. We have not exercised any of those authorities at this point, but there is no way relative to the law or relative to the report language that we can do any of those things unilaterally.

I should also point out that subject to oversight of this committee, with a board that is one-third appointed by the President of the United States, with four or five State entities represented on our board, I don't think it is reasonable to assume that we are going to jump in and suddenly do something that is irresponsible or go into car leasing or something like that.

It is clear in our statute that we are here to provide credit in support of students, period.

Mr. Weiss. Dr. Ingle has not suggested you are going to go into a different line of business. He has suggested you are going to go into competition with him, and that makes his life more difficult.

My question really is premised on the fact that Dr. Ingel suggested it is a year and a half now since he has been having the problem with Sallie Mae and that predates by a year the new authority that was granted to you.

So, that is why I think much of this really may very well be perception, and the perception I think comes about because in fact they have a genuine problem that you are apparently in no position to solve for them at this point.

Mr. Fox. I think we all have to learn how to deal with less—that is a hard thing to accept—less dollars, less support.

Mr. Simon. If my colleague would yield, I think also there may very well be just in part a simple communication problem. I think maybe both at the State agency level, at the Sallie Mae level, you may want to evaluate what you are doing in the way of communication back and forth so that that can improve.

Mr. Ingle. Mr. Chairman, may I respond. I don't have a difference, and I don't wish to get into an exchange. I think that Mr. Fox put his finger on the key issue when he spoke of risk.

The question here is who is going to bear the risk. Is it going to be shared by the general public or is it going to be a private risk. That is part of the question of who is going to pay for, assist in paying for postsecondary education.

I think it is a very important term he has used. I agree with him. I think the point, his suggestion that States are making a lot of money, needs to be kept in mind, that every cent that this program generates is put back into the program. It is a public program for the public interest.

The reference to the $200 million which is outstanding, it is not outstanding. It has been used in terms of commitment. So, I don't think that we have a problem of communication between our two organizations. I think that we, the committee and the general public, have a problem of how to insure credit that is necessary for people to pursue their postsecondary education.

That is the reason I raise these problems. I think it is more than perception.

Mr. WEISS. Isn't it a fact that Sallie Mae no longer has access to Federal moneys?

Mr. FOX. That is correct.

Mr. WEISS. That is a very serious change from what the original source of funds was, which was the U.S. Government.

Mr. FOX. Federal financing, yes, sir.

Mr. WEISS. So now what you have to do is go out to private lending institutions to provide the capital to you. You then have an obligation to make sure the loans you make are sufficiently sound to allow you to pay back the moneys which you borrowed.

Isn't that the way the situation operates at this point?

Mr. FOX. Yes, sir.

Mr. WEISS. So that in fact you do have to be concerned about the risks, Dr. Ingel, involved in this situation. It seems to me that the complaint that you have is a complaint that we have, which is that the Federal Government has again decided that it is easier to shift the burden of risk on to somebody else rather than for it to assume for the broad public that risk.

I share that complaint and concern with you, but it seems that they are just as much the victims in this situation as you are.

Mr. INGLE. I tend to agree with that. I do believe, though—and correct me if I am mistaken—that the current roughly $4.6 billion of capital that Sallie Mae is working from and will be available, what, over the next 14 years or so, is at favorable rates.

The question I guess I am raising here as we discuss who shares this risk is what kind of obligation, if any, is there for that, in effect, special access to capital.

Mr. WEISS. I cannot respond to that.

Mr. SIMON. Do you have any further questions?

Mr. WEISS. I do not.

Mr. SIMON. We appreciate your testimony here. I don't think we are ready to resolve the problem here.

Our final witness today is Mr. Michael Olivas, director of research, LULAC National Educational Service Centers, and chairman of the Hispanic Higher Education Coalition.

STATEMENT OF MICHAEL OLIVAS, DIRECTOR OF RESEARCH, LULAC NATIONAL EDUCATIONAL SERVICE CENTERS, AND CHAIRMAN, HISPANIC HIGHER EDUCATION COALITION

Mr. OLIVAS. Thank you very much.

We appreciate the efforts of you and your staff to allow us to participate.

My name is Michael Olivas. I am the director of research for the LULAC Educational Service Centers, the League of United Latin American Citizens.

I also chair the board of the Hispanic Higher Education Coalition, whose testimony I present today. The coalition is an organization comprised of 13 national Hispanic organizations that represents a very broad scope of interests in the Hispanic community.

I would like to do three things this morning in the time allotted me.

I would first like to share with you some of the general demographic concerns that we have concerning specifically the Hispanic community.

A number of witnesses have spoken in front of the subcommittee over the last years as you fashioned legislation, purporting to speak on behalf of minority interests.

We welcome the opportunity to clarify some of these interests and to read into the record some of those characteristics that do serve to make our community's interests quite different from those of general undergraduate students.

Second, I would like to share largely by inserting into the official record the results of a study on financial aid packaging that we think will reveal quite a few different characteristics and trends.

Mr. SIMON. This is your statement here or this is separate?

Mr. OLIVAS. This will be appended.

Mr. SIMON. They will both be entered in the record.

Mr. OLIVAS. The third thing is to comment specifically on some of the more recent proposals that have been made by the administration concerning Pell grants and loans and what we perceive to be major problems in the delivery of financial aid.

So far we have talked this morning about the delivery of institutional and State and Federal aid. What we are talking about now is on a slightly different level; that is, the direct interaction of Hispanic families with the financial aid system.

Although there is a public perception that minority access in many ways has improved—and due to Federal efforts many of these perceptions are correct—there are some countervailing pressures that have recently caused Hispanic gains, such as they were, to have been eroded.

For example, since 1978 there has been an actual decline in the percentages of Hispanic students at the undergraduate level. We reached a peak of 3.5 percent of all undergraduate enrollments in 1978. It has now slipped to 3.4 percent, despite the larger age cohort for Hispanic students. That is because Hispanic students are disproportionately——

Mr. SIMON. If I may interrupt you, because you are using statistics and I am glancing through your statement—are you including Puerto Rico in the statistics or is it only the 50 States and the District of Columbia?

Mr. OLIVAS. The 3.4 percent to which I just alluded was specifically the 50 States and the District of Columbia. However, I have specific testimony on Puerto Rico. We represent a number of institutions there as well and have participated with a number of Puerto Rican Presidents——

Mr. SIMON. But in your statement, when you talk about any number of things, the maldistribution——

Mr. OLIVAS. Those include Puerto Rican institutions.

Mr. SIMON. OK.

Mr. OLIVAS. You will see, because of the island's inability to participate fully in the political process, there are a number of vulnerabilities that face them that other States and even the District of Columbia do not face, most notably in their ability to raise their own revenue and to cast votes in Congress.

The data are here for the record. I would like to comment only that the salient points are that Hispanic students are for the most part younger than the majority population and, therefore, this is a problem that is not one that is likely to go away.

The underenrollment and attrition of Hispanic students is a problem that will become increasingly important.

We have always been appreciative of your efforts, Mr. Simon, in promoting foreign language study. We think a number of these programs will have their effect if the Federal aid continues to go to the neediest people.

The point I would draw to your attention is on page 21, that in 1976 the median income of Hispanic families was 50 percent less than that of majority families. Yet, while a number of administration proposals continue to insist that only the truly needy will continue to have legitimate claims upon the public purse and support of higher education, we feel a number of the proposals will work directly against this principle.

We feel in particular that the increasing complexity in the delivery of financial aid works to the detriment of less well-educated and poorer families; that is, wealthy families continue to have access to tax preparation assistance, to technical assistance, and to lending institutions that poor families historically have not.

Therefore, the increasing complexity, while it may very well work difficulties with the cash flow of corporations such as Sallie Mae, works in particular to the detriment of families whose incomes are less than $10,000 a year.

This is the median income of Hispanic families, and it is income that in many instances is actually declining due to the size, the larger size of Hispanic families.

On page 4 I have condensed the major findings of a study that the LULAC educational centers conducted over the last 2 years that for the very first time had access to confidential records.

Because of the nature of our work with bilingual counselors, we have been able to gain the confidence and provide taxpayer assistance, as well as financial aid assistance.

We have secured all the necessary forms, but it was very clear that delivery of financial aid to Hispanic students was strikingly different to that for majority students.

In 1979, for example, our sample had two-thirds of the families with incomes of less than $10,500. Less than $10,500 income places them as eligible in almost every poverty program. Furthermore, surely by any definition of truly needy it would include these families as eventual and appropriate recipients.

Of these students, 90 percent received Pell grants, then called BEOG's. Furthermore, 60 percent of these students received only Pell grants. It is very clear in striking contrast to patterns for Anglo students, Hispanic students are predominantly reliant upon need-based aid.

As a matter of fact, in my cohort of freshmen—and I refer you to table 1 appended—it is extremely clear that Hispanic families continue to be needy by any definition of need-based aid.

For the same year, only 31 percent of Anglo freshmen received Pell grants. Over 90 percent of our students received Pell grants in 1979–80 whereas only 31 percent of Anglo students did.

The only program that had major rollbacks over the last 2 years in the actual awards of money were Pell grants, despite very elaborate provisions, very carefully crafted by this subcommittee and approved by Congress for appropriate rollbacks inverse to the basis of need.

Yet, by any definition I would insist these students are the very neediest. For the first time we have evidence that Federal grants have worked to the extent that any need-based aid will, of course, disproportionately help those who are disproportionately poor. By any standard, our group of students is poor.

However, we think that sole reliance upon the major need-based program has worked to the detriment of our students, No. 1, and proposed cutbacks in Pell grants—and I am speaking only of mainland students in this particular data—will work even more to the detriment of students on the island, whose institutions are disproportionately reliant as a proportion of their total income upon Pell grants.

I have some evidence presented by a Puerto Rican resident on page 7 that shows not only the poverty of the island and the disproportionate reliance upon Federal funds, Federal poverty funds, but also the extent to which institutions, particularly private institutions on the island, are reliant upon Pell grants.

Mr. SIMON. May I interrupt you? I apologize for doing this again. I have another meeting that I have to get to. I am going to turn the Chair over to my colleague from New York.

Let me just commend you for your statement. Incidentally, to all the witnesses, we may be submitting written questions. But the problems you have posed are very severe problems.

In the State of Illinois, and I know not too much beyond the State of Illinois, the dropout rate has been significantly high in the Hispanic community. The colleges and universities of Illinois have not responded to specific Hispanic needs as effectively as I think they need to. Back a few years ago I had one meeting with the colleges and universities on that specific problem.

One other point I would just like to make for the record; that is, that whether it is the student program or what it is we cannot treat the people of Puerto Rico as second-class citizens and not expect to invite some instability.

I think one of the areas where we ought to be providing hope for the Hispanic community is through the Pell grant program and the opportunities that we provide there.

I simply want to commend you and apologize again. This is my morning to apologize to witnesses.

Mr. **Olivas**. There is no need, Mr. Simon. I understand you have other duties. We will continue to speak to your staff and to Mr. Weiss. Thank you very much.

Mr. Weiss, I will continue, then.

Mr. **Weiss**. Please.

Mr. **Olivas**. At the same time, it has been acknowledged that financial aid program delivery has become more complex, the administration has proposed in two instances to zero out assisting programs such as Talent Search and education centers, the only programs that do deliver financial aid assistance and counseling.

So, we think while the overall aim to cut costs is of course difficult with which to quarrel, the means by which these cuts would be accomplished will disproportionately affect those people reliant more upon the need-based aid.

I would like to speak from my testimony beginning on page 8 about some of the more recent proposals the subcommittee has heard over the last two weeks.

For instance, in last week's testimony by the Deputy Assistant Secretary of Education it was proposed that current validation efforts "* * * include the requirement that all eligible applicants submit copies of the 1040 tax forms relating to the Pell grant application."

However, it was not mentioned—and we think this is extremely important, and we think as members of Hispanic organizations we can speak to this—that the Tax Code does not require families who live in extreme poverty to file 1040 forms; that is, families who make under the minimum amount required to trigger their filing a mandatory tax form are the only groups that will be required to change their overall practice; that is, we will be in the curious stance of requiring for purposes of validation of needing tax forms that these people's poverty status already precludes them from documenting under the IRS.

So, the only group that would be affected with regard to having to enter the IRS system would be those people who statutorily are exempted from being required to file IRS forms.

While we think this was acknowledged in some of the testimony, we think it was finessed and that it tends to be inconsistent with the insistence by the administration that only the truly needy will continue to have legitimate claims upon these expenditures.

While a debate has been waged in a number of other esoteric places for years, this is the first Federal proposal, to the best of my knowledge, that such students be required to file forms.

Yet, the GAO report itself does suggest, as was alluded to this morning, that the most likely evidence of fraud and underreporting is found in wealthier families, in which you will find Hispanics disproportionately poorly represented.

Therefore, we feel the complexity of the forms, as well as the additional burden of filing IRS forms, for which there is no other statutory mandate for these lower income people to file, will continue to discourage Hispanic families from enrolling.

In our view, this proposal does not reduce paperwork. In fact, it does rather emphatically the opposite. It demands paperwork of people who have no such requirement. Nor do we feel it solves the quality control problems to which it is ostensibly addressed.

In fact, it has been our experience as the largest Talent Search in the United States—we currently maintain 11 Talent Searches, and we have tried to get into New York for several years, but unfortunately there has not been sufficient money to allow us to go through—that we have found the major request for verification on the part of institutional aid officers is when they simply cannot believe Hispanic families could live on so little money; that is, we have had a number of requests from institutions for us to help these families file IRS forms, not because they are required by the IRS, but because the institutions simply cannot believe that families could be so frugal as to live on the amount of money that is a fact of life in Hispanic communities.

While we concede requiring IRS forms would have a major educative value on financial aid administrators who don't have access to carefully commercially prepared financial aid forms which shelter income very nicely, we think this will work once again to discourage disproportionately language minority people, especially low income and Hispanic families.

Financial aid programs are already extremely complex, and as difficult and complex as institutions find them, we would insist that low-income families, particularly those whose families have not gone to college—and Hispanic families have never had historical access to college—it will disproportionately discourage them from encouraging their children from attending.

When the median family income of Hispanic families is 50 percent lower than Anglo families, we think these are the people who will be less likely to perceive that there are credit institutions and loan programs and Pell grants that will continue to assist them, even though their students by virtue of the income would be eligible for these programs.

We feel that the suggestion that the Department be allowed to reprogram $5 million to cover the additional costs ought to be seen for what it is. We believe it is a false economy and it is a shell game. We feel very strongly that this proposal floated up ought to be consigned its proper burial.

We feel also that despite the department's insistence that the truly needy will not be harmed, that the proposals to cut back on TRIO programs and technical assistance preparation programs will work directly opposite to this ostensible intent.

We think that a number of very valuable proposals have been made to increase the cash flow for States to improve the profits of corporations that do lend and guarantee. We have not, however, heard evidence that the truly needy, the neediest in our communities, who would be disproportionately minority, would in any way have their cash flow improved, would have their access improved, nor would be more encouraged to attend college.

We have data that suggests that despite a number of Federal efforts, that the more current efforts, once we have had these children in the pipeline and once through TRIO and other programs, they have been encouraged to stay in high school, we are beginning to see them trail off in college.

We stand ready to assist in any way to answer any questions about more specific proposals that might be advanced about other proposals that while ostensibly helping improve cash flows and fund markets will, we think, work to the disadvantage and detriment of minority students.

We will provide the staff and the committee with our full report, which I think you will find extremely compelling.

For the first time, minority people have studied themselves and we have had access to financial aid records that show unmistakably that Hispanic families tend in many cases to overestimate their income.

As a matter of fact, over 50 percent of the students in my study, which is about to be published by Stanford University, overreported their parent's income by over $500. These children, by virtue of living in our society, cannot believe their families live on so little money.

We think these proposals ought to be seen for what they are: disproportionately harmful to minority communities.

We thank you very much for the opportunity.

[The prepared statement of Michael Olivas follows:]

UNMC APPLICANTS FOR NEED BASED AID

PROGRAM	NO. OF STUDENTS	EST. OF COSTS	FAM./STU. CONTRIBUTION	NEED	FEDERAL		SCHOOL		OTHER		TOTAL AID	UNMET NEED
					WORK/GRANT	LOAN	SCHOL/GRANT	LOAN	SCHOL/GRANT	LOAN		
1981-82					"1981-82 NEED ANALYSIS/AID AWARDED"							
DENTISTRY	100	$1,137,550	$ 466,156	$ 671,394	$ 53,082	$ 678,800	$ 41,891	$ -0-	$ 1,551	$14,500	$ 789,824	$ -0-
MEDICINE	198	1,809,265	609,305	1,199,960	76,806	1,134,100	163,048	$ 14,100	17,870	56,000	1,461,924	
PHARMACY	79	615,000	223,500	391,500	51,818	325,200	12,649	2,000	4,508	-0-	396,175	-0-
GRADUATES	6	57,200	30,950	26,250	1,000	31,800	937	-0-	-0-	-0-	33,737	-0-
ALLIED HEALTH	78	614,400	219,675	394,725	45,613	269,100	14,401	-0-	4,467	19,200	352,781	41,944
NURSING	167	1,108,850	586,400	522,450	123,400	365,050	31,363	1,000	14,327	-0-	535,140	-0-
TOTAL UNMC	628	$5,342,265	$2,135,986	$3,206,279	$351,719	$2,804,050	$264,289	$ 17,100	$42,723	$89,700	$3,569,581	$ -0-
1982-83					"1982-83 PROJECTED NEED/AID RESOURCES"							
DENTISTRY	110	$1,350,000	$ 560,000	$ 790,000	$ 25,000	$ 336,000	$ 45,000	$ 58,000	$ 1,500	$10,000	$ 475,500	$ 314,500
MEDICINE	220	2,200,000	740,000	1,460,000	48,000	427,000	160,000	157,000	18,000	28,000	838,000	622,000
PHARMACY	90	760,000	275,000	485,000	45,000	87,000	13,000	17,200	4,000	-0-	166,200	318,800
GRADUATES	15	140,000	80,000	60,000	-0-	7,000	1,000	500	-0-	-0-	8,500	51,500
ALLIED HEALTH	85	730,000	260,000	470,000	38,000	215,000	14,000	16,700	4,500	10,000	298,200	171,800
NURSING	185	1,340,000	710,000	630,000	90,000	436,000	32,000	7,300	15,000	-0-	580,300	49,700
TOTAL UNMC	705	$6,520,000	$2,625,000	$3,895,000	$246,000	$1,508,000	$265,000	$256,700	$43,000	$48,000	$2,366,700	$1,528,300
EST. $ REDUCTION FROM 81-82'					$105,719	$1,296,050	-0-	-0-	-0-	$41,700	$1,202,881	
% REDUCTION					30%	47%	-0-	-0-	-0-	47%	34%	
1983-84					"1983-84 PROJECTED NEED/AID RESOURCES"							
DENTISTRY	110	$1,350,000	$ 560,000	$ 790,000	$ 12,000	$ 142,000	$ 49,000	$ 5,000	$ 1,000	$10,000	$ 219,000	$ 571,000
MEDICINE	220	2,200,000	740,000	1,460,000	42,000	263,000	165,000	10,000	15,000	25,000	520,000	940,000
PHARMACY	90	760,000	275,000	485,000	28,000	48,000	15,000	2,000	4,000	2,000	99,000	386,000
GRADUATE	15	140,000	80,000	60,000	-0-	1,500	1,000	500	-0-	-0-	3,000	57,000
ALLIED HEALTH	85	730,000	260,000	470,000	23,000	195,000	15,000	2,000	4,000	8,000	247,000	223,000
NURSING	185	1,340,000	710,000	630,000	55,000	400,000	35,000	1,000	12,000	-0-	503,000	127,000
TOTAL UNMC	705	$6,520,000	$2,625,000	$3,895,000	$160,000	$1,049,500	$280,000	$ 20,500	$36,000	$45,000	$1,591,000	[illegible]
EST. $ REDUCTION FROM 81-82 EXCEPT SCHOOL LOAN					$191,719	$1,754,550	-0-	$236,200	$ 6,723	$44,700	$1,978,581	
% REDUCTION					55%	63%	-0-	92%	16%	50%	56%	

ENCLOSURE #4

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PREPARED STATEMENT OF DR. MICHAEL A. OLIVAS, DIRECTOR OF RESEARCH, LULAC NATIONAL EDUCATIONAL SERVICE CENTERS, AND CHAIR, HISPANIC HIGHER EDUCATION COALITION

Many of the recent advances for minorities in higher education are in jeopardy. Despite the public perception that minority students benefited from expanded educational access during the 1960's and 1970's, minority enrollments in higher education remain disproportionately small. The enrollment of Hispanic students has increased in total numbers, but educational parity with majority students or even with other minority students remains an elusive goal. In 1980, Hispanics, representing 5.8% of the mainland U.S. population and 8% of the 18 - 34 year olds, comprised only 3.4% of undergraduate enrollments, a decline from 1978. Further, there is a serious maldistribution within the limited access Hispanic students have had: the public, two year colleges provide the only sector into which Hispanic students have been admitted in significant numbers. Whereas 27% of all white full-time students were enrolled in two year colleges in 1976, 45% of Hispanic full-time students were enrolled in these institutions. Recent research has questioned the equity of such a maldistribution and has suggested that Hispanic attrition is due, in large measure, to the funding patterns and practices that result in Hispanic students having access primarily into two year colleges. This impression is borne out by degree award data, which indicate that while Hispanics receive 4.6% of associate degrees, they receive only 2.1% of masters' degrees and a mere 1.2% of doctoral degrees. Even this limited access has been threatened, as cutbacks have disproportionately affected Hispanics and other disadvantaged communities.

The quality of life for Hispanic Americans is poor, resulting in fewer opportunities for pursuing education beyond high school. Most notably, economic constraints prevent most Hispanics from considering postsecondary education as an option. In 1976, the median income for Hispanic families was $10,259, while the median income for white families was $15,537 (over 50% higher). While 8.7% of non-Hispanic families were below poverty levels, 23.1% of Hispanic families were below poverty level; therefore, in a system of education where financial resources make access more likely, Hispanics are at a severe disadvantage.

Even if formal economic barriers did not preclude Hispanic participation in postsecondary education, informal barriers to success would still prevent significant Hispanic enrollments. First, the public elementary and secondary school systems into which Hispanic students are placed do not provide adequate attention to cultural and linguistic needs of Hispanic children. Clearly, this situation keeps the pool of Hispanic high school graduates low and provides inadequate preparation to those who do complete their course of study. Second, Hispanic youths are inhibited in their pursuit of higher education by the scarcity of informational structures that would help them negotiate existing barriers. Because high school counselors are rarely able to provide adequate information to Hispanic high school students, these students are left to secure information from whatever source may be available to the minority community, which has little access to financial resources. Parents, who usually would be of assistance to their children in college selection, are major sources of encouragement, information, and financial support. Hispanic parents, however, themselves denied college opportunities, are less likely than majority parents to be able to negotiate information systems for their children. Third, existing systems of college support services that appear to be equitable on the surface subtly result in inequitable practices. For instance, extensive governmental loan programs will include parental or student negotiation with banks or credit institutions where credit history and experience are required. Many minority families have not had extensive experience with these loan institutions and may be intimidated by what seems to be mortgaging their future.

STUDENT FINANCIAL AID: HISPANIC ACCESS AND PACKAGING POLICIES

Financial aid is essential to disadvantaged students, and is the major governmental investment in postsecondary education. This testimony reports the findings of an ongoing national project on financial aid packaging for Hispanic students, the first such study ever conducted to analyze Hispanic student financial aid awards. Data problems have plagued earlier packaging studies, as national data bases have relied upon students' estimates of family income and their memories of financial aid received. Employing program data from the LULAC National Educational Service Centers, an 11-city Hispanic counseling organization, this study is based upon IRS returns and parent confidential statements notarized to be correct indicators of family income. To record student awards, aid report forms were secured from institutions. A sample of 521 Hispanic full time, first time freshmen, enrolled in 1979-80, was assembled; all files were audited for completeness and documentation. The sample replicated the institutional-type enrollment patterns of Hispanics and Mexican/mainland-Puerto Rican subgroups.

The most striking single finding is the small extent to which any packaging is being performed: over sixty percent of all the students received only one source of aid, almost exclusively Basic Educational Opportunity Grants (BEOG's, since 1981 known as Pell Grants). BEOG as a major component of multiple sources was also evident, for 90% of multiple sources included a BEOG award. Single-source aid was evident at all income levels, ranging from 54% of lower-middle to 65% of upper-middle students.

The evidence of little packaging for Hispanic students contrasts both with earlier studies of Hispanic student aid and with current packaging practice for all students. In 1972-73, fifty two percent of Hispanic aid packages were single sources, but only 23.4% of all packages were solely grant awards; there was evidence that work study (10.3%), loans (14.7%), and benefits (3.7%) were significant components of Hispanic financial aid packages, at all income levels and for attendance at all types of institutions. A 1978 study of student assistance reported that even students from the lowest income families attending the least expensive schools averaged $158 of non-grant federal aid in their average package of $1,079. Data from 1979 revealed that only 31.5% of all freshmen received a BEOG, only 7.2% a SEOG, and 13.2% a guaranteed student loan. It is clear, then, that grant aid has risen dramatically for all students, in all institutions and for all income levels. These Hispanic data, however, reveal a strikingly different pattern in the students'extraordinary reliance upon grants, to the near exclusion of other forms of aid.

The data were also disaggregated by median family income and the type of institution attended. Crosstabulations show several trends: in each income quartile, more money went to students attending, in descending order, private four year, private two year, public four year, public two year colleges. Additionally, students from low and lower-middle income families received more aid than did students from upper middle and high income families; curiously, however, except for students in public two year institutions, in each institutional type, lowest income students received less aid than did students in the lower-middle category: the mean difference was more than $200 per student. One of the assumptions of financial aid distribution is that the neediest students receive the most assistance, within the limits of institutional costs. It could have been expected, then, that within institutional types, the amounts to students would slope downward, with the highest aid awards going to the students in the lowest income category. In these data, only the public two year colleges showed such a pattern, with private four year colleges showing a disturbing tendency to award more aid to higher income students.

Despite the favorable income slope, attending a public two year college meant that students were less likely to receive aid. Fewer students attending public community colleges received aid than did students attending other institutions, and in the important grant category, a significant difference in grant receipt was evident. This lower availability of financial assistance corroborates other research on the practice of community colleges in financial aid administration. This finding is more enigmatic in light of the heavy reliance by public two year colleges upon federal financing for their Hispanic students, and cannot be explained by the institutions' lower costs. Public two year colleges are the sector most reliant upon federal financial aid, and the sector with the least discretionary aid. This reliance upon federal funds is a major shift since Hispanic packaging data in 1972-73, when the federal sources of aid were 39%, non-federal 21.6%, and mixed sources 39.4%. Inasmuch as Hispanic students are disproportionately enrolled in public two year colleges, this distribution of assistance suggests that enrollment patterns may inhibit complete access to financial aid resources; the extraordinary reliance upon federal funds may also mean that federal cutbacks in financial aid programs will disproportionately affect community colleges and Hispanic students.

While Puerto Rican students on the island were not included in this study, Pell cutbacks will hurt Puerto Rican institutions even more than those in the 50 States and D.C. Not only is poverty more devastating in Puerto Rico than elsewhere, but the political status of the island leaves it extremely vulnerable in the Congress, and its inability to tax itself fully removes the fall back provisions available to States. The 131,054 postsecondary education students in Puerto Rico are part of a total population of more than three million people, most of whom have incomes below the poverty level. As of October 1978, 55 percent of all families were participating in the Food Stamp Program, and 78 percent of them received the food stamps for nothing. The annual disposable income per capita for 1980 was $1202 at constant dollars as of 1954. As of January, 1981 the unemployment rate in Puerto Rico was 18.9.

Approximately 90 out of every 100 students are eligible for financial aid. For the 1980-81 fiscal year the student financial aid from the federal government constitutes about 93 percent. Student financial aid is very important for private institutional survival. Ninety-six percent of the institutional income from tuition and fees in private institutions comes from student aid. Because of these characteristics, Puerto Ricans will be harmed by proposed cutbacks, and will not be able to use traditional political forums. This will have severe repercussions for the island economy and stability.

"Quality Control" and Disadvantaged Families

While the Administration's aims at reducing regulatory burdens are laudatory in the abstract, in practice they will work to the detriment of low income families. For instance, in last week's testimony by the Deputy Assistant Secretary of ED, it was proposed that current validation efforts "include the requirement that all eligible applicants submit copies of the 1040 tax forms relating to the Pell Grant application."

A scholarly debate on this topic has been politely waged in academic journals for many years, but, to my knowledge, this is the first federal proposal that such additional paperwork be required of Pell grant applicants. In our view, this proposal collapses under its own weight. It neither reduces paperwork, nor does it solve the quality-control problems alluded to in earlier testimony.

In fact, the Department's study itself suggested that overpayment was likelier to occur in wealthy families, whose access to technical assistance and tax-reduction advice effectively shelters disposable income. Even though the study is severely flawed in many respects, its findings do not suggest that low income families systematically misreport their income -- and the LNESC study showed extraordinary accuracy among Hispanic low income families, both for dependent and independent students. In fact, it has been the LNESC experience, as the country's largest Talent Search, that most institutional verification audits are initiated by financial aid officers who are skeptical that families can live on so little money. In short, the reality of Hispanic and other minority poverty cannot be believed by aid administrators.

While the verification may prove to be of enormous educative value to these administrators, we are confident that requiring IRS forms for all students would disproportionately and detrimentally affect minorities. First, lowest income families -- are not required to file IRS returns; the number of persons not required by IRS to file returns is expected to increase this year, due to increased unemployment and larger numbers of public assistance families. These persons -- by any yardstick the "truly needy" -- would be required to file 1040 forms merely to verify their Pell applications.

Financial aid program applications are already complex enough to require arithmetic and literary skills far beyond the levels of most disadvantaged families. Additionally, poor families have far less disposable income to spend upon technical assistance that is more readily available to wealthier families. Moreover, even the GAO's recent report notes that inaccurate reporting of income is likeliest with wealthy families, whose complex deductions and complicated returns in no way resemble the returns of low income families. In our view, the additional requirement would dissuade minority families from sending their children to school, the opposite effect of the Administration's proposal.

Finally, even if this proposal had a compelling public policy that did not harm minority access, other departmental actions have significantly reduced minority gains. As noted, previous Pell Grant cutbacks, ignoring rollback statutes, disproportionately affect minority students. The Department has proposed, in last week's testimony by the Undersecretary, to reprogram over $5 million in Pell appropriations to pay for these additional paperwork burdens. To do so would not only continue to rob students of program money, but would constitute a tacit admission that RIF's in the audit divisions have left the Department without adequate personnel to monitor its own radical policy shifts. Such false economies should be seen for what they are, shell games that will continue to hurt minority students.

That the Administration is insensitive to minority access is not only clear from its program proposals, but from its budget figures. Even if the increased paperwork were legitimate and all students were required to submit 1040's, technical assistance for financial aid applications have been eliminated from the Department's plans. For FY 1982, the Department requested no funds for Talent Search or Education Opportunity Centers, whose counseling programs reached thousands of low-income students each year. These zero-funded programs and severe cutbacks in other TRIO programs will serve, in tandem with increased administrative hurdles, to undermine the limited access Hispanics and other minorities have earned.

While majority organizations have purported to have minority interests at heart, Hispanic organizations urge this subcommittee, if it is serious about preserving programs for the truly needy, to reject these proposals and to maintain the supportive services that enable disadvantaged students to participate in postsecondary education.

Financial Aid:

Access and Packaging Policies for Disadvantaged Students

Michael A. Olivas

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ABSTRACT

Financial aid is essential to disadvantaged students, and is the major governmental investment in postsecondary education. This paper reports the finding of an ongoing national study on financial aid packaging for Hispanic students, the first such study ever conducted to analyze Hispanic student financial aid awards. Because confidential records of a national Hispanic counseling program were used, exceptional detail and accuracy were possible. The study details the composition of awards, the proportion of reimbursable aid, family contributions, student quality indices (GPA, test scores), and choice of curriculum. One major finding is that Hispanic students are overwhelmingly reliant upon governmental, not institutional, funding and that nearly 3/4 receive only one kind of aid. Finally, the paper presents models for aid awards based upon public policy objectives and recommends several packaging policies for use by aid administrators.

Despite its importance in the administration of financial aid, little is known about packaging policy. Billions of dollars each school year are distributed through public and private programs, and nearly all colleges and universities assemble financial aid "packages" for students, whose eligibility is computed by third party form-processors. Yet, even with major investments in financial assistance -- and increasing research and policy analyses on the topic of financial aid -- scant attention has been paid to the economic, equity, or policy dimensions of packaging. This omission is anomalous, for the major federal higher education legislative debates have been over financial aid, whether establishment of massive grant and loan programs, the expansion of these programs to "middle-income" students, or current Republican efforts to trim back costs in the financial aid programs [16].

In all these activities, there is an assumption that institutions employ a logic in their packaging and administration of various assistance programs assembled into a single account or "package" upon which a student draws. A national financial aid study group accurately labeled packaging as "the moment of truth when it all comes together, where the broad funnel of aid resources comes to its narrowest point and those resources delivered to the student" [39]. Significant institutional and national social policies are also effected by packaging techniques, even if these policies are unarticulated or inconsistent among students' packages. For example, packaging can be used as a tool for redistribution: "Packaging as a process is important because through it inequities of the student aid system can potentially be corrected" [21]. Packaging is also a means for planning the use of institutional resources [29,43]and for improving choices for students to consider a wider range of institutions [12,33]. There is also evidence that certain packaging policies may work to increase student enrollments and retention [2,31], while other studies have found little or no such impact upon retention [24,26].

Neither research nor policy analysis, however, has resolved what are fundamentally societal questions: what societal goals should be furthered by packaging policies; and what administrative means should be used to further these policies? National study groups convened to examine these financial aid issues have an uneven record in addressing packaging policies. The 1971 Panel on Student Financial Need Analysis [43] analyzed the fundamentals of packaging, noting that different types of aid have different characteristics for student recipients and institutions, and outlining several techniques for packaging -- each with different political and philosophical underpinnings. A 1973 HEW Task Force on Management of Student Assistance Programs attempted to identify acceptable guiding principles for distribution of financial aid; the Task Force noted that any of the principles "might guide the effort to secure effective coordination and interconnection of the six student assistance programs. However, the existence of several similar but yet distinctive concepts has instead served more to confuse matters, perhaps even deterring the development of a fully-coordinated approach to the award of various student assistance monies" [22]. The National Commission on the Financing of Postsecondary Education report, also published in 1973, did not address packaging [37], nor did the Commission's 1974 policy research report [38]. The National Task Force on Student Aid Problems report, drafted in 1975, echoed earlier findings in the HEW Report, and concluded that a major purpose of packaging was "to redress inequities caused by a random and uncoordinated national system of financial aid distribution" [39].

Researchers, therefore, have had little record of public debate on packaging issues, even as the complex federal and state financial aid procedures have further clouded research issues. Because there is no national consensus upon packaging, institutions have wide discretion to combine resources according to institutional priorities and policies, even within governmental and College Scholarship Service guidelines; therefore any large scale study of packaging policies will be limited by complex and difficult-to-define institutional features. An even more serious deterrent to packaging studies has been the extensive data problems inherent in such an undertaking.

Due to problems of confidentiality of student records, disparaties between student-reported items and accurate figures, poor minority data, and underenrollment of low-income students, no national study has emerged that has managed to overcome these formidable obstacles. Confidentiality rules, intended to protect student records from invasions of privacy, have meant that institutions will not allow researchers access to award files [17,47]. The major alternative has been to mine major longitudinal or large scale student data sets, such as the National Longitudinal Study (NLS) [34,50], the Cooperative Institutional Research Program (CIRP) [2,4,5], or Higher Education Panel (HEP) [6]; while these data bases afford considerable opportunity to study student samples, they rely upon student estimates of family income and financial aid received, as well as upon student-reported characteristics such as grade point averages and standardized test scores. Particularly for low-income students, these measures frequently are inaccurate and there are many non - response items that must be controlled [13,20,50]. Moreover, the data bases often are inadequate to measure minority student characteristics, as they do not sufficiently oversample minority populations or account for minorities' maldistribution throughout the postsecondary education system [3,41]. Finally, national surveys can have major order effect liabilities, as the thousands of respondents infer different meanings from complex items [46].

Data

Of course, no data set is without limitations, particularly if one wishes to study a minority population. For Hispanics, who have not been well sampled in student surveys [3,42], the longitudinal data bases have provided only partial insights into packaging. However, a data base for Hispanic student packaging has been developed by a national community-based counseling organization, whose records have proven to be an unobtrusive measure for studying financial aid for Hispanic students. The organization, the country's largest Talent Search -- a federally funded counseling program -- has offices in 11 cities located in every region of the country with large Hispanic populations. Established in 1973, the organization counsels over 16,000 students each year, two-thirds from disadvantaged backgrounds and approximately 85% of them Hispanic or other minorities. Each of the 11 centers has full-time counselors who assist the students and their parents in completing scholarship or financial aid forms and college applications. Because of federal recordkeeping requirements for the program, extensive data are gathered for each student; due to the complex nature of financial aid applications, many personal and family items are necessary, including parental income and other confidential data. Finally, in order to follow-up with students, the organization requires that students share financial aid information with counselors after enrollment, so official institutional award notices are filed with student records. This process, intended to meet program counseling requirements, has yielded an extraordinary and serendipitous data base of financial aid data for 1979-80 Hispanic full-time students that overcomes many of the formidable problems with the use of student surveys in packaging studies.

Moreover, the locations of the counseling offices in 11 cities combine to approximate a sample of the three major Hispanic subgroups: Mexican Americans (60%), Puerto Ricans (15%), and Cubans (6%) [14,Table 1.01]. Because the organization opened a Miami office midway through the 1979-80 program year, these data are predominantly Mexican-American (Chicano) and mainland Puerto Rican enrollments; in the future, however, the Miami files will yield additional Puerto Rican and Cuban students. Of the full-time, first time Hispanic student files, every tenth file of each counselor's caseload was pulled, until 20 files per counselor were available. Edit checks were performed to ascertain completeness, documentation (eg., transcripts, parent confidential statement, award report), and ethnicity. The only item imputed was test scores for students who had not taken standardized tests; approximately 30% of the files required such imputation, derived from a method that assigned a score to students within income categories [23,50]. Because there is a large body of literature on SAT score measures, composite ACT scores were converted by SAT percentiles [35,36]. A total of 521 complete files was compiled, each containing a 30-item counselor questionnaire, notarized parental confidential statement or IRS return, a high school transcript, an official test score (except where scores were imputed), a notification of aid award, and other personal information such as letters or application essays.

Family income guidelines for the Talent Search Program require that at least 2/3 of those clients served be from low-income families [28]. Minority families tend to be more economically disadvantaged than white families, and in 1977, non-Hispanics had a median income almost $1,000 higher than that of Hispanics, particularly Chicanos and Puerto Ricans [14,Table 1.12]. With program guidelines and Hispanic poverty, it was not surprising to find that 77% of the students in the sample came from families with 1978-79 incomes of less than $15,000; over 60% of the families had incomes of less than $10,500. It must be remembered that these data were compiled from notarized statements and IRS tax returns, avoiding the errors of student reporting of family income. While it is possible that persons misreported or misrepresented their earnings, IRS returns are considered good measures of income; if their confidential nature is not abused, they are exceptionally good unobtrusive measures [46]. Each file was coded with a FICE (Federal Interagency Committee on Education) identification number, so institutional data could be obtained from FICE tapes. Where indicated, financial data are in 1979-80 constant dollars; any adjustments for inflation are noted parenthetically. Income quartile measurements conform to 1972 NLS categories of low (below$7,500), lower middle ($7,500-$10,500), upper middle ($10,500-$15,000) and high (over $15,000), even though inflation has rendered these terms meaningless. That over half of the students in the data base came from families with a 1979 median income of less than $10,500 -- when in 1972 such income was considered "lower middle" -- confirms the extent of poverty in Hispanic communities and attests to the need to target Talent Search services upon such economically disadvantaged populations.

The balance of this paper analyzes the findings of these data, noting in particular the patterns of aid awards, the "packages" of Hispanic students; it also attempts to measure the relationships between student characteristics and financial aid received. It examines institutional financial aid administration policies in assembling packages for Hispanics, and assesses the impact of governmental aid policies upon these students. Finally, it discusses models for aid awards based upon public policy objectives and recommends several packaging policies for use by aid administrators. There is a popular ideology that suggests "need-based" awards help economically disadvantaged students, and the data examined in this study both support and refute this ideology.

Given the inchoate nature of the ideology and the inconclusive nature of previous packaging research, this study has as its purpose the establishment of current baseline data on receipt of financial aid by disadvantaged Hispanic students. Moreover, an attempt to formulate early models of packaging policies is made. So little data-based research on packaging has been attempted that no compelling theoretical frameworks have emerged; another reason why packaging "theory" has been so atheoretical is that many institutions treat their financial aid administration mechanically (frequently on a first-come-first-served basis) rather than theoretically or philosophically.

Research Findings

① The most striking single finding is the small extent to which any packaging is being performed: over sixty percent of all the students received only one source of aid, almost exclusively Basic Educational Opportunity Grants (BEOG's, since 1981 known as Pell Grants). BEOG as a major component of multiple sources was also evident, for 90% of multiple sources included a BEOG award. Single-source aid was evident at all income levels, ranging from 54% of lower middle to 65% of upper-middle students receiving only one source of aid. The pattern of single source aid by SAT scores is less evenly distributed across all score levels, due both to the imputation of scores for non-testtakers and to the few students (34) with combined SAT scores above 950: the lowest score category had 62% of its students with single-source aid, while the three higher score categories ranged from 44% to 77% with single-source aid -- almost exclusively BEOG and Supplemental Educational Opportunity Grant (SEOG) awards.

(Insert Table One)

The evidence of little packaging for Hispanic students contrasts both with earlier studies of Hispanic student aid and with current packaging practice for all students. In 1972-73, fifty two percent of Hispanic aid packages were single source, but only 23.4% of all packages were solely grant awards;

there was evidence that work study (10.3%), loans (14.7%), and benefits (3.7%) were significant components of Hispanic financial aid packages, at all income levels and for attendance at all types of institutions [50,Table IV-15]. A 1978 study of student assistance reported that even students from the lowest income families attending the least expensive schools averaged $158 of non-grant federal aid in their average package of $1,079 [19,Table 4.17]. The 1979 CIRP data revealed that only 31.5% of all freshman received a BEOG, only 7.2% a SEOG, and 13.2% a guaranteed student loan [5,pp,57-8]. It is clear, then, that grant aid has risen dramatically for all students, in all institutions and for all income levels. These Hispanic data, however, reveal a strikingly different pattern in the students' extraordinary reliance upon grants, to the near exclusion of other forms of aid.

Table Two disaggregates the data by median family income and the type of institution attended. Crosstabulations show several trends: in each income quartile, more money went to students attending, in descending order, private four year, private two year, public four year, and public two year colleges. Additionally, students from low and lower middle income families received more aid than did students from upper middle and high income families; curiously, however, except for students in public two year institutions, in each institutional type, lowest income students received less aid than did students in the lower middle category: the mean difference was more than $200 per student. One of the assumptions of financial aid distribution is that the neediest students receive the most assistance, within the limits of institutional costs. It could have been expected, then, that within institutional types, the amounts to students would slope downward, with the highest aid awards going to the students in the lowest income category. In these data, only the public two year colleges showed such a pattern, with private four year colleges showing a disturbing tendency to award more aid to higher income students.

(Tables Two and Three)

Despite the favorable income slope, attending a public two year college meant that students were less likely to receive aid. As Table Three indicates, fewer students attending public community colleges received aid than did students attending other institutions, and in the important grant category, a significant difference in grant receipt was evident. This lower availability of financial assistance corroborates other research on the practice of community colleges in financial aid administration [7, 25, 30; for an opposing view see 40]. This finding is more enigmatic in light of the heavy reliance by public two year colleges upon federal financing for their Hispanic students, and cannot be explained by the institutions' lower costs. As Table Four shows, public two year colleges are the sector most reliant upon federal financial aid, and the sector with the least discretionary (non-federal) and mixed-discretionary aid. This reliance upon federal funds is a major shift since Hispanic packaging data in 1972-73, when the federal sources of aid were 39%, non-federal 21.6%, and mixed sources 39.4% [50, Table IV-20]. Inasmuch as Hispanic students are disproportionately enrolled in public two year colleges [41], this distribution of assistance suggests that enrollment patterns may inhibit complete access to financial aid resources; the extraordinary reliance upon federal funds may also mean that federal cutbacks in financial aid programs [16] will disproportionately affect community colleges and Hispanic students..

Conclusions and Policy Implications

In the main, the data in this study reveal that financial aid is being distributed to Hispanic students on the basis of "need." The distribution system evidently is working, if the index is that lower income students are to receive larger aid awards. However, while this equitable principle is a fundamental premise of financial aid distribution, it is surely not the sole criterion. Student choice among institutions, public support to the private sector, human capital investment, and aid to "middle income" families are just as surely premises of the existing financial aid system. Susan Nelson has succinctly summarized these indices: "In short, what is the standard against which the actual distribution of student aid can be judged? There is no clear answer to this question, though the choice of a standard crucially affects the verdict" [40, p. 1].

It may be that a single standard does not exist, as crucial as the choice of standard clearly is. And while politically glib justifications for aid to education and increased financial aid programs may invoke the "societal good" rationale, less debate has centered upon *which* societal good is to be subsidized and which not. The passage of the Middle Income Student Assistance Act typified the view that "middle income" families deserved more support; of course, the $25,000 annual income mischaracterized as "middle income" showed more clearly that upper income recipients were the students Congress had in mind to assist. This belief, however, and its enactment into legislation indicate the difficulty in introducing theoretical concerns into educational finance issues, particularly student financial assistance programs. Just as the excessive costs of medical education have called into question the federal investment into subsidizing more medical schools and doctors, so are massive quasi-entitlement programs such as BEOG's and student loan authorities being reexamined by budget cutters [16].

Unfortunately, the budget cutters have no more theoretical framework for financing higher education or for delivering student aid than did the programs' founders. The rollbacks in BEOG's (from $1800 to $1750 to $1670) have ignored the legislation's rollback provisions that mandated rescissions inversely related to need, and have shown no theoretical approach to the program - - perhaps the most legislatively-pure need based aid program in postsecondary education. Cutbacks over the last few years in nursing "capitation" grants have occurred despite seeming shortages of nurses. Higher unemployment among the educated seems to have undercut upward mobility and higher occupational status as an end of education. However, at a time when fundamental educational fiscal issues are being debated, packaging theory remains ignored, even though the assembling of financial aid at the institutional level holds promise as a major redistributive public policy intervention point.

Consider several packaging scenarios, based upon different public policy fiscal presumptions. Assume that higher education is determined to be an individual good, the benefits of which accrue solely to the recipient. In such a case, self-help or reimbursable aid would be the appropriate packaging strategy; work-study, loans, and personal resources (which may include family savings) would be packaged, and loan terms could be arranged so that the government did not subsidize deferred repayment. A second scenario assumes that a more highly educated citizenry is a social benefit, and that education for all persons is an external consideration. This presumption would entirely subsidize tuition, living expenses, and perhaps foregone income. No self-help, save participation in the tax system, would be required, on the assumption that this scheme would subsidize itself over time. Yet another scenario, a variation of the second case, would reward persons with certain characteristics, on the assumption that society needed to educate more of these persons, whether honor students, minorities, veterans, doctors, or whichever characteristics were deemed worthy of subsidization. This more targeted social benefit theory could use packaging as a focused mechanism for achieving the good. Many other such scenarios could be envisioned either in pure or mixed versions, and financial aid packages could be assembled to effectuate the policies by indexing awards to choice of curriculum, grade point averages, student characteristics, or a mix of qualifications.

These scenarios do exist and are routinely employed by institutions for assembling millions of packages each year. [See 51 and 52 for more comprehensive treatment of these fiscal issues.] However, as noted earlier, the magnitude of the administration of awards and the lack of consensus on aid or packaging principles have precluded more thoughtful theoretical approaches to public policy on student financial assistance. Several packaging models are summarized, according to the mix of aid and public policy objectives:

(Insert Figure One)

Anyone familiar with higher education institutions will recognize Case IV, the mixed purpose package, as the most common type of aid award, reflecting several purposes and delivery systems. Yet the Hispanic data detailed in this study reflect almost a pure II or III, depending upon whether grants are characterized as societal benefits or targeted group benefits. In truth, they are both. It is also true that BEOG's, as the cornerstone of federal higher education policy, are a major component of wealthier students' packages. This role does not reflect ambivalence as much as it reflects the mixed purposes (and mixed economy) federal policies reflect in the financing of student assistance. Always reluctant to legislate in language explicitly spelling out "minority" entitlement, Congress has frequently employed "need" as a criterion, even when majority students have disproportionately participated [41, 42, 51]. If administered well, such indirection may yet improve minority access.

FIGURE ONE

I. Individual Benefit

- work study
- unsubsidized loans
- personal and family resources

II. Societal Benefit

- subsidized grants
- subsidized loans
- no charges

III. Individual or Group Characteristic Benefit

- subsidized grants according to specific characteristic
- loans subsidized according to specific characteristic
- personal resources indexed according to specific characteristic

IV. Mixed Purpose Packages

- work study
- loans
- grants
- award for characteristics
- personal and family resour

Even if the verdict is that lower income Hispanic students fare relatively well, there are clear signs within these data that the maldistribution of students throughout the postsecondary system and the high reliance upon single source federal aid could augur problems. While the data base replicates the distribution of Hispanic students by institutional type, the concentration of students in two year institutions raises serious concerns about widespread access to the system; moreover, the concentration is even more striking when it is known that 21 institutions enroll a quarter of all Hispanic students in the 50 states and D.C. [14, p. 119]. The public two year colleges are the most dependent upon federal aid, exceeding even "other" schools such as proprietary and postsecondary adult basic education centers (Table Four); these institutions use less discretionary aid in Hispanic packages, owing to little endowment or institutional aid resources. Because needy students will only attend institutions where they receive an aid award, Hispanic students may be dissuaded from attending private four year colleges where aid is more readily available to wealthier students and more discretionary institutional aid awards are made. Moreover, the low SAT scores and large percentage of Hispanics who do not take standardized tests may preclude the students from being eligible for most private four year institutions, unless colleges are willing to employ other criteria, including alternative qualitative indices.

Another problem may be the extraordinary reliance of Hispanic students upon BEOG's almost to the near-exclusion of other forms of aid. The dangers are twofold: government cutbacks in BEOG's and unpackaged aid's effect upon student persistence. BEOG awards have been scaled back from a maximum of $1,800 in 1979-80 to $1,670 in 1981-82 [16], and institutions not accustomed to packaging aid awards may require Hispanics to make up the difference by parental contribution or summer earnings. With the poverty and lack of summer job opportunities for minority youth, this gap may not be made up by all students. In particular, two year colleges continue to underutilize campus-based financial aid programs [25,40]. Equally serious, the lack of comprehensive, multi-source packages may have a detrimental effect upon Hispanic persistence. There is compelling evidence that different types of aid facilitate persistence, for reasons that are not fully understood [2, 32]. College work study participation, in particular, seems to improve the likelihood that students will remain in school, perhaps because the regular earnings require students to budget their money (whereas grants made in lump sum do not force such frugality), or because the contact with a supervisor makes students feel a part of the system, or because a meaningful skill is acquired.

It is difficult to recommend an increased emphasis upon loans, as the 1972 evidence suggested Hispanic students took on disproportionately large levels of indebtedness [18, Table 5.17[. Although these data reveal small participation in loan programs, institutions frequently use loans as an increasingly large share of packages, on the assumption that the longer a student is in college, the larger the share of reimbursable aid should be. If this unarticulated packaging is in effect, then data on Hispanic juniors and seniors may reveal more participation in loan programs. Even though these data differ significantly from CIRP baseline data on freshman packages, what may be operating is institutional decisions to award Hispanics - - who tend to have lower grades, test scores, and persistence than do majority students - - grant packages that do not require reimbursement or take time that could be used for study. Inasmuch as Hispanic students tend to come from lower income families and to express more economic concerns than do majority students,* aid administrators should consider whether moderate work study or cooperative education programs might afford more psycho-social benefits than merely awarding single source BEOG packages. The federal cutbacks may force such considerations upon colleges, and aid administrators should work with institutional researchers to assess the effect of packaging upon low-income students.

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*Data on high school seniors show considerable differences between white and Hispanic student concerns. Hispanic seniors expressed more concern over money peoblems (45.5% to 27.4% for white students) and family obligations (39.3% to 23.6%) [14, Table 2.16].

One obvious limitation of these data is that only enrolled students are studied, and there is no practical way to know how many students were discouraged from attending college because of their inability to receive technical assistance, to negotiate the aid application process, or to secure aid. However, it is intuitively obvious that students from low-income families have fewer resources to spend on college, and in many ways, the aid system compensates for this imbalance by making larger awards to needier students. Concentrating upon those Hispanic students who do make it into the system ought not blind educators to the major access barriers that remain, or lull observers into believing that the financial aid system - - however equitable towards needy students - - can itself remedy historic exclusion. Nonetheless, it is evident that financial aid packaging can be a powerful means of increasing access to postsecondary education.

TABLE ONE

Distribution of Financial Aid According to Type of Aid, by Family Income and SAT score, For Entering Full-Time Freshmen Students

	Total Aided Freshmen	Single type only				More than one typ	
		Grant	Work	Loan	Benefit	With Grant	Without Grant
All Aided Freshmen	100 (521)	60.0 (313)	* (1)	* (1)	* (4)	34.7 (181)	4.0 (21)
FAMILY INCOME QUARTILE[a]							
Low	232	59.4 (138)	* (1)	* (0)	1.2 (3)	33.6 (78)	5.1 (12)
Lower Middle	82	52.4 (43)	* (0)	* (0)	1.2 (1)	42.6 (35)	3.6 (3)
Upper Middle	88	64.7 (57)	* (0)	* (0)	* (0)	31.8 (28)	3.4 (3)
High	119	63.0 (75)	* (0)	* (1)	* (0)	33.6 (40)	2.5 (3)
SAT SCORE[b]							
Low	430	60.2 (259)	* (1)	* (1)	* (4)	33.9 (146)	4.4 (19)
Lower Middle	57	63.1 (36)	* (0)	* (0)	* (0)	36.8 (21)	* (0)
Upper Middle	25	44.0 (11)	* (0)	* (0)	* (0)	52.0 (13)	4.0 (1)
High	9	77.7 (7)	* (0)	* (0)	* (0)	11.1 (1)	11.1 (1)

* = less than 1.0%

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[a] Income quartiles calculated from student-reported income interval estimates: Low = less than $7,500; Lower Middle = $7,500 to $10,500; Upper Middl $10,500 to $15,000; High = over $15,000.

[b] Students are grouped according to SAT-equivalent scores; Low = less tha 800; Lower Middle = 800 to 950; Upper Middle = 950 to 1,100; High = over 1,10

TABLE TWO

Average Total Aid Received by Entering Full-Time Freshmen Aid Recipients by Median Family Income and Institution Type and Control

MEDIAN FAMILY INCOME

MEAN TOTAL DOLLARS STD DEV	UNDER $7,500	$7,500 $10,500	$10,500 $15,000	$15,000 & over	ROW TOTAL
INST TYPE					
PUBLIC 4-YEAR	2251 204862 1287	2530 75914 1383	1725 65536 1196	1406 88597 1014	1959 43490 1290
PUBLIC 2-YEAR	1805 176936 1190	1476 41321 1037	1109 35495 750	[illegible] 35151 742	1[illegible]82 [illegible]96 [illegible]91
PRIVATE 4-YEAR	3243 42162 1919	4356 43564 2541	4705 37637 1799	3514 49202 1933	3835 17256 2081
PRIVATE 2-YEAR	2885 37504 886	3301 13205 543	2333 11667 1439	2409 7228 1332	2784 69604 1016
OTHER	1859 31610 1189	1971 19711 1222	2145 10727 1347	1998 3995 420	1942 66043 1152
COLUMN TOTAL	2125 493074	2362 193715	1830 161062	1548 184173	1981 1032024

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TABLE THREE

Financial Aid Recipients According to Type of Aid, by Institutional Type and Control*
(Percentage Distribution)

Mean (count)	Financial Aid	Grants or Scholarships	Term-time Earnings	Loans	Benefits
Public 4	(222)	92.4 (219)	22.8 (54)	21.1 (50)	4.2 (10)
Public 2	(195)	83.6 (178)	2.8 (6)	1.4 (3)	9.9 (21)
Private 4	(45)	95.6 (44)	21.7 (10)	32.6 (15)	2.2 (1)
Private 2	(25)	96.0 (24)	12.0 (3)	4.0 (1)	8.0 (2)
Other	(34)	85.3 (29)	0.0	11.8 (4)	11.8 (4)
Total	(521)	89.0 (494)	13.2 (73)	13.2 (73)	6.8 (38)

*Horizontal percentage totals may exceed 100%

TABLE FOUR

Distribution of Financial Aid According to
Federal Source, by Institutional Type and Control,
For Entering Full-Time Freshmen
(Percentage Distribution)

% distribution (count)	Federal only	Non Federal and Federal	Non Federal only
Total (521)	63.5 (331)	31.8 (166)	4.6 (24)
Public 4 (222)	61.3 (136)	34.7 (77)	4.1 (9)
Public 2 (195)	78.5 (153)	19.5 (38)	2.0 (4)
Private 4 (45)	26.6 (12)	55.6 (25)	17.8 (8)
Private 2 (25)	16.0 (4)	80.0 (20)	4.0 (1)
Other (34)	76.5 (26)	17.6 (6)	5.9 (2)

TABLE FIVE

Packaging of Federal Aid to Aided Entering Full-Time Freshmen by Student and Family Attributes

STUDENT/FAMILY ATTRIBUTE	PERCENT OF AIDED FULL-TIME FRESHMEN			
	Total Aided Freshmen	Receiving Federal and Non-Federal Aid	Receiving Federal Aid Only	Receivin Non-Feder Aid Onl
All Aided Freshmen	521	33.0	63.5	3.5
FAMILY INCOME QUARTILE[a]				
Low	232	30.2	67.7	2.2
Lower Middle	82	42.7	56.1	1.2
Upper Middle	88	31.8	63.6	4.5
High	119	32.8	60.5	6.7
SAT SCORE[b]				
Low	430	31.2	67.2	1.6
Lower Middle	57	38.6	52.6	8.8
Upper Middle	25	44.0	36.0	20.0
High	9	55.5	33.3	11.1

[a] Income quartiles calculated from student-reported income interval estimat Low = less than $7,500; Lower Middle = $7,500 to $10,500; Upper Middle = $10,500 to $15,000; High = over $15,000.

[b] Students are grouped according to SAT-equivalent scores: Low = less than Lower Middle = 800 to 950; Upper Middle = 950 to 1,100; High = over 1,100.

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APPENDIX

Regressions were computed for data described in the study, but were not reported because they tended to replicate patterns already shown by the crosstabulations. Several of these computations suggest further work with logit or profit analysis, and are therefore included as an appendix. Interested persons should contact the author for correlation matrices, a list of variables, and other data.

APPENDIX I

Fractional Standard Deviation Increase in Receipt of Financial Aid (for One Standard Deviation Decrease in Family Income)

Sample	Dependent Variable	Fractional S.D. Increase in Receipt of Financial Aid (significance level)
Chicanos	AIDTOT	.31 (.01)
Puerto Ricans	AIDTOT	.00 (NS)

AIDTOT = Total Aid Received
NS = Not Significant at .05

APPENDIX II

Fractional Standard Deviation Increase in Receipt of Financial Aid (for One Standard Deviation Decrease in Family Income), by Institutional Type

Sample	Dependent Variable	Fractional S.D Increase in Recei of Financial A (significance lev
Two year Colleges		
Chicanos	AIDTOT	.46 (.01)
Puerto Ricans	AIDTOT	-.08 (NS)
Four year Colleges		
Chicanos	AIDTOT	.30 (.01)
Puerto Ricans	AIDTOT	.18 (NS)

AIDTOT = Total Aid received

NS = Not significant at .05

APPENDIX III

Fractional Standard Deviation Increase in Receipt of Financial Aid (for One Standard Deviation Increase in Institutional Cost), by Institutional Type

Sample	Dependent Variable	Fractional S.D. Increase in Receipt of Financial Aid (significance leve
Chicanos	AIDTOT	.51 (.01)
Puerto Ricans	AIDTOT	.39 (.01)
Two year Colleges		
Chicanos_	AIDTOT	.18 (.01)
Puerto Ricans	AIDTOT	.54 (.01)
Four year Colleges		
Chicanos	AIDTOT	.61 (.01)
Puerto Ricans	AIDTOT	.12 (NS)

AIDTOT = Total Aid Received

NS = Not significant at .05

Mr. WEISS. Thank you very much for your testimony. We do look forward to the receipt of the full study when it is available to us.

Let me ask you, why do you believe that there is this smaller by far percentage of full financial aid packaging for Hispanic students? Why are there not as high a percentage of students who are receiving information and making applications for the guaranteed student loans, for example?

Mr. OLIVAS. My study was of full-time freshmen, and freshmen are frequently less likely to have major elements of a loan package any way. Although the 1978 study did show even for students from the lowest income, Anglo students, over 10 percent of their packages were traditionally non-Federal assistance, which would include in some cases State assistance.

We think that institutions only recently have become aware of the underenrollment of Hispanic students, in large part because we do not have a network of historically Spanish institutions comparable to those of other communities.

So that there is not perceived to be a cadre of students because of the perceptions which are incorrect—in New York you know it is particularly incorrect to assume that Hispanics are predominately a Southwest phenomenon. After all, there are more Hispanics in the State of New York than in my own home State of New Mexico.

Mr. WEISS. I always thought it was in New York.

Mr. OLIVAS. There are other reasons as well. We think institutions in many cases have relied only upon Federal assistance in the packaging; that is, they feel because of Federal efforts to make minority education a higher priority, that the institutions will use their own money, but because there is need-based data, because minorities are disproportionately needy in the financial sense, that it is not inappropriate for them to package aid with predominately Federal sources.

However, I would note since 1972, when the first BEOG grants were given, that Hispanic students' reliance upon Federal assistance has practically tripled. So we think there is clear evidence that institutions at least rely upon Federal largesse for enrolling minority students, whereas they do not rely on the same sources of aid in assisting majority students.

A second thing is need-based aid will go to the neediest students. Hispanics, being disproportionately needy, will receive that aid and our disproportional enrollment in 2-year colleges, where there are no dormitory facilities and, therefore, lower cost, will also tend to keep the cost down for our students.

I might add that that has not worked to the advantage of our students. So the disproportionate effect of proposition 13 in California on the 2-year sector, the only sector hurt in the first year because of its reliance upon property taxes, has hurt an enormous number of Hispanic students.

Over one-third of all Hispanic undergraduates on the mainland are from California, so as California's resources for community colleges declines, it declines disproportionately for Hispanic students.

That is why our insistence that demographics have precluded fuller understanding of the problems facing our students. We felt this was the appropriate forum for sharing some of these demographics.

Mr. WEISS. It is important. I share your perception that in all likelihood a lot of the students who receive the BEOG's really don't need or don't need as high a percentage of additional aid. So that of necessity, by definition, there would not be even the need for further packaging, let alone the awareness that it would be available.

Mr. OLIVAS. The need is, of course, a difficult debate but it is less debatable that need is there. It is not clear why the assumptions are that families will have the resources to make up the difference. Hispanic families, by virtue of the size and poverty of the family, simply do not have funds available.

Yet, you would be surprised, as you and your staff review our findings, that our families are making disproportionately large investments of their liquidity, such as it is. It just happens there is less of it.

We now feel that liquidity will have to go toward getting taxpayer assistance, even where they are not required to file IRS forms, so they will have to avail themselves of these services even though the IRS statutes would not require them.

Mr. WEISS. Well, I would like to see that information, too. In New York, of course, we have in addition to the Federal grant program a State grant program. That again is not uniform across the country.

I would assume, too, that your statistics would probably indicate that more of by far the Hispanic students attend institutions in their home States than the general population, and because of that the costs would be lower because again across-the-board costs for residents at most of the State institutions is much lower than for people from out of State.

Mr. OLIVAS. That is true. The TAP program has been extremely well-used by Hispanic students. We credit the State for its generosity. We think it is an excellent long-term investment.

As for the willingness to attend schools outside of State, while it is generally perceived this may be cultural parochialism on the part of Hispanic students, we think it is far more a function of the very small numbers of our parents who have been educated in prestigious schools and therefore we don't have access to the alumni and automatic admissions that many private schools have, the networks of alumni recruiting that other communities have had.

Second, we also feel that the poverty in our community simply precludes the ability to consider schools outside of living at home and attending a community institution. You have heard testimony by community college representatives that continue to cite this as an example.

We think your subcommittee has an excellent opportunity in its defense of TRIO programs to insure that the information be given to students, that they have a wide range of numbers of institutions that they may attend.

It is particularly important for New York administrators and educators to recall the number of Puerto Rican students from the island who do attend because of the number of family they have in the State of New York.

So, the migration from the island to New York continues to help Hispanic students enroll in schools apart from their immediate home area.

Mr. WEISS. Well, I suspect that the food stamp amendments that we adopted last year are going to help in that regard, too.

Do you have any view as to whether the cutbacks in the loan programs also affect Hispanic students?

Mr. OLIVAS. The data I have shared with you only includes freshmen students, because we have found once our students are at least in college and out of high school they are there to stay. We concentrated only upon the freshmen students.

There is considerable evidence, unfortunately anecdotal, our own experience, that a number of States and lending institutions have residency requirements which are appropriate, but they also have previous banking requirements that preclude families who are not already existing customers of those lending institutions to become so, in some cases up to a year before they are eligible to participate in those programs.

We think this works against low-income families who have so little liquidity that in many cases there is no reason to participate in IRA, Keogh plans, savings plans, checking plans, and so forth.

In many cases their bills will be paid in cash or directly with the agency because it is less expensive than to maintain the monthly checking charges and because increasingly a number of lending institutions require a certain amount of deposit in order to participate in checking plans.

We think these practices, as well as the very clearly documented unwillingness of many lending institutions to loan mortgage money to people who live in minority communities, are less likely to be willing to go out of their way to lend money.

So, we anticipate in our followup these freshmen students will be encountering more difficulty as they progress through college.

We have also found from a 1972 study that had major data problems but nonetheless showed by the time Hispanic students graduated from college they had 10 percent higher levels of indebtedness than Anglo students.

So, it is apparent the institutions, once they have felt the students are safely enrolled, have increased the amount of loans and because Hispanic families have not traditionally had the opportunities to negotiate purchases and to arrange their finances, because there is so little liquidity, that we will increasingly find evidence that Hispanic families have been actively discouraged or in many was subtly discouraged by lending institutions who have no previous credit dealings with these populations.

We also find relatively few loan officers who are bilingual and who can negotiate with the parents in many cases to mortgage their home or to put down the collateral that is necessary.

I draw your attention to the fact that the median income of Hispanic families is $10,000, which is less than the cost of education in leading institutions. It is very difficult to explain to these families there will be need-based aid to enable their son or daughter to attend college.

So, we anticipate the cutbacks in TRIO programs in particular, which provide the information and the counseling that enables the students and their parents to understand the processes, will not even allow our families to get to the level of discussion about whether or not one State or another has sufficient loan guarantees.

We are interested in getting our students into colleges and keeping them there. We think a number of the proposals, while ostensibly concerned for the truly needy, will in fact work just the opposite.

Mr. WEISS. It has been my experience—not just in this area, but across the board—that advocacy groups from within the affected communities are the most effective in getting the message out and being persuasive in having legislation tailored in effect to meet the real needs of the particular community.

I know there has been a tremendous increase in effective advocacy within the Hispanic community. I assume you see that effort growing and becoming even more effective. Indeed, I assume your participation here with us is part of that ongoing effort.

Mr. OLIVAS. We would like to think that is the case. We would like to have opportunities to articulate our perspectives more and have access to research sources to study our own populations. We feel that monolingual English speakers would not be able to conduct the studies we did.

However, we also feel that we don't have the margin of error other communities do in that sense. The issues are very real. The University of Puerto Rico and other colleges down there have had considerable unrest that we think is going to give other students and institutions pause if they see now how the cutbacks have affected one group of people who are politically powerless in the sense they are not able to vote in Congress.

So, we are optimistic in the sense that our numbers are growing and that public policy consideration has been accorded us. However, people continue to see this as a new problem. That is simply not the case. We are more able to articulate our points of view.

Proposed cutbacks, particularly in TRIO programs, would literally devastate a number of Hispanic organizations who have by virtue of their not being tied to institutions been able to provide the very information that enables students to have a range of choices.

So, Talent Search, for example, administered by institutions, tend to have a loyalty to the institution that provides their overhead whereas our students range from community colleges they may wish to attend by virtue of their family's financial situation, all the way to more prestigious institutions that may be outside their State.

In the private sector we have been focusing upon scholarships. The League of United Latin American Citizens, for example, has always administered scholarships now, over 50 years.

The Hispanic Higher Education Coalition and its member organizations have a number of scholarship funds, and we do this because of the historical perception that institutions themselves will not be sensitive to our students and our families simply do not have the resources available that majority families have relative to our students.

So, we have always stressed the need. We just have not had the opportunity or the forums where we could articulate these perspectives.

Mr. WEISS. Thank you.

Does either counsel have questions?

Ms. MCADAM. On page 5 of your testimony you make a statement that within institutional types the lowest income students are receiving less aid than lower middle income groups. Now, you went on to explain there are differences on how great that was, depending on institution types.

Did your data show any reason why that is true?

Mr. OLIVAS. I would refer you to table 2, which actually shows that. We can only speculate because although we had the cooperation of a number of institutions, financial aid decisions were made on a number of bases, not always well articulated and in many cases purely administrative.

I would draw your attention to the top line in each of the institutional types. The premise of financial need is that the neediest will get the most. Yet, you will find that the only sector in which that properly operates is the public 2-year sector. Those are the poorest students, whose families come from under $7,500, receiving $1,805, sloping down to $1,400.

We are particularly concerned about the private 4 year data because private 4-years are frequently perceived to be the most prestigious institutions. There you will see that the poorest students—those are the ones in the lefthand column—received $3,200 a year. It ranges all the way to $4,700, to families that are wealthier. Then it goes down again if they are extremely wealthy. We would have expected just the opposite.

We are not precisely sure what the explanation is. We of course hope to follow it up. The data are quite clear because we had IRS forms. This was not students reporting what their parents made. These were actual figures, verified in every case, and not students simply recalling what financial aid they got, but institutional reports of what they were.

So, we think on both ends of the study our data are better than previously published data. We can only speculate that 2-year colleges take their tasks more seriously in enrolling low-income students. They take all comers and provide aid when they did. They have less reliance, particularly in California, upon Federal aid because there is no tuition in a number of the 2-year colleges.

However, this also takes into account other expenses of attending college. Even when students do not live on campus there are costs associated with maintenance that should be taken into account. We would like to explore that anomaly a little more thoroughly. We are seeking money from private sources that would enable us to do so.

We are particularly concerned that the consideration is so bad. It is again like being overly dependent upon Pell grants. That is the only one being cut back in all amounts. If the 2-year colleges are the ones that have the least access to discretionary money, that is their own institutional resources, and that is where our students are, they are less likely to have much packaged aid, whereas if our students go to Yale or more heavily endowed schools, the institutions are more likely to give them institutional assistance because the gap between Federal assistance and the need is going to be larger.

It has to be made up by some source. If they are serious about keeping their students, they consider them good investments. Bilingual students that graduate from college are exceptional investments.

Mr. **Dean**. What percentage of Hispanic students receiving Pell grants are receiving the maximum Pell grant?

Mr. **Olivas**. The total I believe was approximately 80 percent.

Mr. **Dean**. Do you also want to supply this for the record. If the Congress were to pass legislation reducing the maximum grant say to $1,200 or $1,300, what impact would you project that would have on educational opportunity for Hispanic students.

Mr. **Olivas**. I think we have that evidence in decline in enrollments from 1978 to 1979. Our kids are the most marginal with regard to their economic resources. Not only does word of cuts spread fast, but that there are more to come spread faster.

Because our students are not having access to other institutional resources, the word gets out very quickly that if Pell grants are cut, "I will not be able to attend college." We have seen that, and we think the difference between 1978 and 1980 in enrollments manifests that exactly.

Mr. **Dean**. One final question.

Of the Hispanic students who complete a 2-year course in a community college, what percent of them actually pursue additional education after graduation?

Mr. **Olivas**. Transfer data are very difficult to get. I have some data I would be glad to share in book form, published by the Howard University Press, a book I wrote on the topic. I would give you two indices to give you the figures: 4.8 percent of all associate degrees are awarded to Hispanics and 2 percent of all bachelor's degrees are awarded to Hispanics.

The attrition, in my view, is roughly equivalent to that. Whereas the enrollments and graduation rates in associate degree programs, predominately in 2-year colleges, are approximately the age cohort; that is, you would expect, given the demographics on the mainland Hispanic students, given the relative youth, would be about 5 percent. However, you would expect the investment in Federal and State resources would have led to a greater production of bachelor's degrees.

What we do find, those students who do go on graduate in numbers that are actually higher than Anglo students who transfer. It is misleading, however. What we find is with up to 40-percent attrition rates at the high school level, we are getting the cream of the crop.

Mr. **Dean**. OK. Thank you very much, Mr. Chairman.

Mr. **Weiss**. Dr. Olivas, thank you very much for your important, significant testimony.

The record will be kept open for you to submit additional material, if you so deem appropriate, for the next 10 days.

Again, thank you very much.

Mr. **Olivas**. Thank you, Mr. Weiss.

Mr. **Weiss**. I am sure we will be in touch as the year goes along.

The subcommittee stands adjourned subject to call of the Chair.

[Whereupon, at 12:40 p.m., the subcommittee adjourned, subject to call of the Chair.]

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